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IN THE

Supreme Court of the United States

OCTOBER TERM, 1963

No. 684

THE SUPERIOR OIL COMPANY,
Petitioner,

v.

FEDERAL POWER COMMISSION,
Respondent.

PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

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FEDERAL POWER COMMISSION,

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PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

The Superior Oil Company (Superior), Petitioner in the proceeding below, prays that a writ of certiorari issue to review the judgment of the United States Court of Appeals for the Ninth Circuit entered in The Superior Oil Company v. Federal Power Commission, on September 25, 1963.

OPINIONS BELOW

The opinion of the Court of Appeals for the Ninth Circuit is reported in 322 F. 2d 601. Such opinion and the Court's Judgment are reprinted herein as Appendix A (*infra*, pp. 1a-41a). The Order of the Federal Power Commission (Commission), issued June 15, 1962, is reprinted herein as Appendix B (*infra*, pp. 43a-44a). This Order was affirmed by the Court below.

JURISDICTION

The Original Opinion of the Court of Appeals was entered on August 26, 1963. Petition for Rehearing en banc was denied by further Opinion issued September 25, 1963, amending the original opinion without changing the ultimate conclusion. The judgment was entered October 15, 1963. The jurisdiction of this Court is invoked under 28 U.S.C. 1254 (1) and Section 19 (b) of the Natural Gas Act, 52 Stat. 831 (1938); 15 U.S.C. Sec. 717r(b); herein called "the Act".

QUESTIONS PRESENTED

The Commission, without hearing, summarily rejected: (a) Superior's application for Certificate of Public Convenience and Necessity (actually for an amendment of a previously issued certificate to include additional gas from a lease in the same field to be sold under the original contract); and (b) Superior's rate filing related to such certificate filing (a change in rate schedule being an amendment of the original contract to include the additional acreage), which presents the following questions:

I.

Where the substantive regulatory authority of the Commission derives wholly from Sections 4, 5 and 7 of the Act, and these sections authorize the exercise of such authority only in the light of the statutory standards of just and reasonable, and the requirements of present or future public convenience and necessity determined after a hearing;

(a) Can the Commission in any case reject, without a hearing, a rate filing or a certificate application which complies with formal filing requirements?

(b) Can the Commisson, authorized to make rules and regulations necessary or appropriate to carry out the provisions of the Act, determine by general rule that no hearing will be granted on certain certificate applications and rate filings if they contain substantive matters deemed objectionable by the Commission?

II.

Where a regulating statute provides for unlimited rate filings, except as restricted by contractural provisons, may the Commission prescribe contract provisons which would restrict the filing of possible future rate changes and proscribe other contract provisons which would allow less restricted possible future rate changes.

III.

Where the Federal Power Commission is required by Congress to conduct hearings upon all certificate applications filed to determine whether they are required by the present or future public convenience and necessity, and the statute prescribes no situation which per se may not be so required, may said Commission promulgate prospective general rules which deny a hearing and reject applications because of substantive matter therein contained?

IV.

Where a regulatory commission is by statute authorized to review rate changes filed with it to determine after a hearing whether such rates are just and reasonable and to make rules and regulations necessary or appropriate to carry out the provisions of such statute, can such commission validly promulgate general rules of prospective appli-

cation which require rejection without hearing of certain rate change filings merely to reduce its administrative burden?

V.

May the Federal Power Commission under the Natural Gas Act and its authority to make rules necessary or appropriate to carry out the provisions of that Act validly promulgate a general rule which (a) enlarges its regulatory authority, (b) does not reasonably accomplish the stated purpose of the announced rule and (c) is unreasonable, arbitrary, capricious and discriminatory in application?

STATUTE AND RULES INVOLVED

The pertinent provisions of the Natural Gas Act, 52 Stat. 821ff (1938), as amended by 56 Stat. 83 (1942), by 62 Stat. 991 (1948), by 63 Stat. 107 (1949) and by 72 Stat. 947 (1958), 15 U.S.C. Sections 717-717w, are set forth in Appendix C (infra, pp. 45a-52a). They are Section 4 (a), (b), (c), (d) and (e), Section 5 (a), Section 7 (c), (d) and (e), Section 16 and Section 19 (b), 15 U.S.C. 717c (a-e), 717d (a), 717f (c), (d) and (e), 717o and 717r (b).

Order No. 242, Amending Regulations Under the Natural Gas Act (18 CFR 154.93, 157.14, 157.25) is set forth in Appendix F (infra pp. 63a-67a) preceded by related Orders No. 232, Appendix D, and No. 232 A, Appendix E (infra pp. 53a-62a).

Section 1.7(b), Rules of Practice and Procedure, (18 CFR 1.7 (b)), is set forth herein in Appendix G (infra pp. 67a, et seq.)

STATEMENT OF THE CASE

This is a proceeding to review the action of the Commission summarily rejecting without hearing the filing by Superior of its Supplement No. 8 to Gas Rate Schedule No. 77, and its Amendment to Application for Certificate of Public Convenience and Necessity, both dated May 25, 1962.

Under Section 4 of the Act schedules of all rates and charges relating to a jurisdictional sale of natural gas must be filed with the Commission; and under the Commission's Regulations the gas sales contract involved and all amendments thereto constitute the "rate schedule". No change in any rate schedule may become effective without thirty days prior filing. The Commission may permit such filed change to become effective or suspend it and institute a hearing to determine its justness and reasonableness.

Under Section 7 of the Act, no jurisdictional sale of natural gas may be commenced without a Certificate of Public Convenience and Necessity issued by the Commission after a hearing and based on a finding, supported by substantial evidence, that such sale is required by present or future public convenience and necessity.

Under review here is a Letter-Order dated June 15, 1962, issued by the Commission's Secretary without a hearing summarily rejecting an application for certificate, and a rate filing by Superior, occasioned by a contract supplement adding acreage from which gas is to be sold to a previously certificated contract. Said supplement makes no change in the prior contract except to add additional acreage in the same field from which gas was to be sold to the originally certificated Buyer at the same price and terms. Such filings were (1) an Application for an Amendment of a previously issued Certificate of Public Convenience and

Necessity and (2) a Notice of Change of Rate Schedule. The original contract had been accepted by the Commission as Superior's Rate Schedule No. 77 and a certificate issued for the sale thereunder. Said original contract and the covering certificate had on two prior occasions been supplemented in identical fashion for the same purpose, and the related certificate amendments and rate changes had been duly accepted by the Commission.

Superior's Application for Rehearing and Reconsideration of the rejection order, filed July 9, 1962, (R-123), was denied by the Commission's inaction, again without a hearing. This filing pointed out the defects of such order under the Act and the due process clause of the Fifth Amendment to the Constitution, because it was based on Order 242 which was subject to the same defects, and requested rehearing.[1] The only reason stated by the Letter-Order rejecting Superior's filings was: "The supplemental agreement appears, therefore, to incorporate by reference pricing provisions other than those permitted by Section 154.93 of the Commission's Regulations. Therefore, in accordance with Commission Order No. 242 * * * the proposed rate schedule supplement and related petition to amend are hereby rejected". (R-120) Order No. 242 (27 F.R. 1356) is shown herein as Appendix F (*infra*, pp. 63a-67a).

This order is thus clearly unlawful unless Order 242 is one that the Commission may validly make, without a hearing, as necessary or appropriate to carry out the provisions

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[1] It is significant that the Court below (pages 6a, 22a, 25a, 27a, 34a,) made much of the fact that Superior did not separately petition for amendment or repeal of order No. 242 under Sec. 1.7 of the Commission's Rules of Practice and Procedure. Superior in said petition clearly pointed out the unlawfulness of said Order No. 242 as urged below and herein, and by implication sought repeal of said order or rule.

(Secs. 4, 5 and 7) of the Act, and unless said Order is reasonable in its application here. We, therefore, look at Order 242, and its background. Under date of April 4, 1956, the Commission issued a Notice of Proposed Rule-Making (21 F.R. 2389) in Docket No. 153. Such Notice proposed to amend Section 154.93 of the Regulations under the Natural Gas Act (18 C.F.R., Sec. 154.93), to provide that contracts containing certain price changing provisions would not thereafter be accepted for filing as rate schedules. The contract provisions specified in the Notice were "(a) escalation clauses based on price indices or changes in the prices received by the purchaser on resale, or (b) the payment or offer of payment of higher prices by the purchaser or other purchasers in the same or other producing areas to the same or other sellers". For convenience these clauses are designated: (a) changes based on economic conditions and resale prices, and (b) "favored nation" clauses. Comments were permitted, and in fact filed up to June 1, 1956. After receipt of such comments, the Commission took no further action in this proceeding for five years.

On March 3, 1961, after a hearing in which The Pure Oil Company was the only producer party, the Commission issued its Opinion No. 341, *In the Matter of The Pure Oil Company*, 25 FPC 383, in which it found that favored nation clauses were contrary to the public interest, but were not invalid, and further that the circumstances involved, as reflected by that record, did not "trigger" the particular price increase proposed by Pure.[2] The same day the Commission without further notice in R-153, issued its Order No. 232 (25 FPC 379 Appendix D, *infra*, pp. 58a-58a) in the

[2] The reviewing Court affirmed the Commission's construction of the favored nation clause "on the record", and agreed that in the light of such construction such clause had not been activated. *Pure Oil Company* v. *F.P.C.* (7 Cir. 1962), 299 F. 2d 370, 373.

long dormant rule docket, basing its action not upon "administrative hearings" in Docket R-153, but upon the *Pure* record and opinion.

Order No. 232 provided that as to contracts tendered for filing after April 3, 1961, the contract provisions listed in its Notice of Rule-Making five years previously and *all other* price escalation provisions would be "inoperative and of no effect at law" except (1) those for fixed amounts at fixed dates, and (2) those to reimburse the seller for tax increased paid. As Commissioner Kline said in his dissent, "no showing has been made that all outlawed clauses are against the public interest" (*infra*, p. 58a). Interested parties were allowed seventeen additional days in which to submit further views concerning said Order; and in response to such submissions, on March 31, 1961, the Commission partially reversed its prior position by declaring that the elimination of all indefinite pricing provisions would be so restrictive that the industry could not adequately cope with possible changing economic conditions over the span of long-term contracts, and issued Order No. 232A (25 FPC 609, Appendix E, *infra*, pp. 59a-62a). This amended Order permitted contracts dated on and after April 3, 1961, to contain provisions permitting the parties to redetermine the price during a five-year period if and only if there was no other provision in the contract for a price change during such period, and if such redetermination was based upon and not higher than jurisdictional prices previously approved by the Commission for other sales in the area. This Order has been held to be a general declaration, non-adjudicatory of rights, and not subject to judicial review. *Sun Oil Company* v. *F.P.C.* (5 Cir. 1961) 304 F. 2d 293, cert. den. 371 U.S. 861.

On October 10, 1961, the Commission issued Notice of Rule-Making in Docket R-203 (26 F.R. 9723) proposing that contracts containing any price changing provision other than those expressly permitted by Order No. 232, as amended by Order No. 232A, would be rejected as rate filings or as supporting the gas supply requirements of pipeline applications or as exhibits for producer certificate applications. Comments were again permitted and received. Under date of February 8, 1962, in Docket R-203, the Commission issued Order No. 242 (27 FPC 339, Appendix F, infra, pp. 63a-67a) purporting to act under the authority of Sections 4, 5, 7 and 16 of the Act. Again, reliance was placed solely on the record in *Pure, supra.* This order provided that the Commission would reject contracts dated after April 2, 1962, with provisions other than those approved by Order No. 232A, whether filed as rate schedules of Sellers or in connection with applications for certificates of Sellers or Buyers. The Commission recited, from its prior Orders Nos. 232 and 232A, (which had then been held non-reversible, *supra*) that indefinite escalation clauses have no apparent relation to the economic requirements of the producers who file changes under them and generalized upon the burdens cast upon it due to such filings.

This Order was also held not subject to review; because the petitioners had not attempted to file with or use before the Commission any contract executed after April 2, 1962, containing a proscribed provision, and therefore were unaggrieved by the order. *Hunt Oil Company* v. *FPC*, and *The Superior Oil Company* v. *FPC*, (5 Cir. 1962) 306 F. 2d 878; *Texaco, Inc.* v. *FPC* (10 Cir. 1963) 317 F. 2d 796, 804. Neither Orders Nos. 232, 232A nor 242 were based on a hearing of evidence.

Superior in the instant proceeding has never had a hearing or an opportunity to support its filings; and it has never had an opportunity to present evidence to show the unreasonableness and arbitrary effect of Order No. 242 or that same is not appropriate or necessary to carry out the provisions of the Natural Gas Act. Had Superior been granted a hearing in the rule proceedings, it would have shown that the economic principles which control the gas producing industry and which control Superior's present and future operations, and the financial requirements of Superior, present and future, require the "indefinite" price provisions of the types proscribed by said Orders Nos. 232A and 242 and included in the instant filings, and that such provisions are fair, just and reasonable. Had Superior been granted a hearing on the instant filings, it would have shown by evidence that the particular provisions included in the instant contract are required by present and future public convenience and necessity, and that the same are required to meet its financial requirements and will produce rates, present or future, which are only just and reasonable.

REASONS FOR GRANTING THE WRIT

The decision below is in conflict with the decisions of the Court of Appeals for the Tenth Circuit on the same matter in *Texaco, Inc.* v. *FPC* (10 Cir. 1963) 317 F. 2d 796, 804-807,[3] and the conflict is acknowledged in the Court's opinon (*infra*, pp. 24a and 34a). The decision below is also in conflict with the decision of the Court of Appeals

[3] The Opinion of the Ninth Circuit Court refers to this Tenth Circuit decision as "Pan American Petroleum Corp. v. Federal Power Com'mn," *infra*, pp. 24a and 34a; but the West Federal Reporter System labels it "Texaco, Inc. v. Federal Power Commission".

for the District of Columbia in *Willmut Gas and Oil Company* v. *FPC* (D.C. Cir. 1961) 294 F. 2d 245, 249-250, cert. den. 368 U.S. 975, 82 S. Ct. 477. In addition, said decision conflicts with the statutory scheme of regulation established by the Act as interpreted by this Court in *United Gas Pipe Line Company* v. *Mobile Gas Service Corp.* (1956) 350 U.S. 332, 76 S. Ct. 373 (Mobile), *United Gas Pipe Line Company* v. *Memphis Light, Gas and Water Division* (1958) 358 U.S. 103, 79 S. Ct. 194 (Memphis) and *The Atlantic Refining Co.* v. *Public Service Commission* (1959) 360 U.S. 378, 79 S. Ct. 1246 (Catco). Finally, said decision determines an important question of federal law which has not been but should be settled by this Court —, the extent of authority, if any, of an administrative agency (such as the Federal Power Commission) to exercise complete regulatory authority by general rule-making without hearing when the granted regulatory authority is provided to be exercised only after a hearing. This is a problem exceeding mere academic interest. The issues involved plumb the depths of constitutional due process of law.

1. In the *Texaco* case, *supra*, the Commission, as here, had summarily rejected a contract for filing under the authority of Order No. 242. The Tenth Circuit reversed the action of the Commission, holding such rejection and Order No. 242, the basis therefor, invalid, because: (1) there is no statutory authority for the summary rejection of contracts under Sections 4, 5 and 7 of the Act, and the general rule-making power set out in Section 16 "is not a source of power to regulate in conflict with the substantive provisions of the Act" and thereby create "a legislative change", but only empowers the Commission to make rules and regulations *to*

carry out the provisions of the Act. (2) The Commission by general rule-making order may not substitute its standards for those prescribed by the statute. (3) The Commission may not successfully maintain that such general orders are not subject to direct court review, and then in reliance on such orders reject certificate applications and rate filings, because such is a "boot strap operation" which "deprives natural gas companies of their statutory right to a hearing, ignores the statutory standards, and precludes the possibility of any effective judicial review". (4) The Commission may by quasi-legislation fill "interstices" in the Act, but it cannot usurp Congressional power by expanding the authority granted to it by the Act on a claim of need to be relieved of an administrative burden created by the Act itself.

The Court below expressly acknowledged disagreement with the Tenth Circuit Court (*infra*, pp. 24a and 34a) and held that (1) since in "rule making there is no constitutional requirement for any hearing whatsoever" under Section 16, which authorizes rules "necessary or appropriate to carry out the provisions of this act", the Commission could by general rule exercise the substantive regulatory power granted it under Sections 4, 5 and 7, notwithstanding that under said sections "hearings are concededly required". (2) The rule making power of the Federal Communications Commission which is couched in the same terms as that of the Federal Power Commission, *i.e.*, rules necessary or appropriate to carry out the provisions of the Act, is no greater than that of the Federal Power Commission, notwithstanding that the Communications Act[4] expressly establishes classes of appli-

[4] The Communications Act of 1934 (as amended), 47 U.S.C. 301 et seq.

cants who shall not be licensed, *i.e.*, multiple ownership cases where licensing would tend to lessen competition or restrain trade; while the Natural Gas Act sets up no group or class of applicants whose proposals may not be found to be required by public convenience and necessity or whose rates may not be found to be just and reasonable. (3) That statutory and constitutional requirements for evidentiary hearings prior to any administrative determination of public convenience and necessity or justness and reasonableness of rates are satisfied by a Commission regulation allowing the filing of a petition for the amendment or repeal of a Commission rule which deprives one of such hearing opportunity. (4) That administrative findings supported by evidence are not required to support either a general rule determining substantive matters or the specific application of any such general rule, if the administrative body states in the general rule order "that it intended" to accomplish an object "rationally related to * * * regulatory objectives embraced by the statute * * *".

2. In addition to the acknowledged conflict with the Tenth Circuit, the decision below conflicts with *Willmut, supra.* The District of Columbia Court of Appeals held unequivocally that Section 16 of the Act "does not authorize an order, rule or regulation which would nullify or restrict the right of a natural gas company to change the rates under which it offers to furnish service". 284 F. 2d 245, 250. The Court below held this not applicable to a prospective rule which restricts the right to change rates. Of course, total lack of power is not improved or added to because its attempted exercise is only prospective rather than retroactive.

3. The decision below conflicts with the "comprehensive and effective regulatory scheme" established by the Act as interpreted by this Court in *Mobile, supra, Memphis, supra,* and *Catco, supra.*

Mobile, 350 U.S. 332, at 338-343, and *Memphis,* 358 U.S. 103, at 112-114, held that the Act does not "abrogate" nor "affect" the pre-existing right of natural gas companies to contract for rates and rate changes to govern their services. The Act gives the Commission only the power to initiate a hearing to review such agreed on rates or rate changes and to determine the justness and reasonableness thereof after they have been filed with the Commission. The Court below held that the Commission by general rule may prospectively prescribe and proscribe contract provisions as to which the parties may agree. This certainly abrogates and affects a natural gas company's right to contract for its rates, and is totally inconsistent with authority only to review rates after they are filed with the Commission. The Commission's Order No. 242 limits both the right to fix and change rates by contract.

This Court in *Catco,* 360 U.S. 378, at 392, held that the Commission may place reasonable conditions upon the granting of a certificate in order "that the consuming public may be protected *while the justness and reasonableness of the price fixed by the parties is being determined under other sections of the Act*". (Emphasis added.) So holding, this Court again recognized the right of natural gas companies to contract for and have reviewed under the standards of the Act, i.e., just and reasonable, any rate for which such companies should see fit to contract. The Court below held that contract rate provisions and the provisions permitting changes in rates can be restricted by general rule

to only those previously and without hearing found innocuous by the Commission.

4. The Court below determined an important question of federal law, i.e., — What, if any, limit exists to the exercise of substantive regulatory authority by the Federal Power Commission under its general rule making power, where such general rule is promulgated without a hearing. This question has not been but should be settled by this Court.

The Court below admitted that all authority for the contested orders must be found in Sections 4, 5 and 7 of the Act. The Court further admitted that each of these sections authorizes regulatory action only after a hearing, but then held that the general rule-making power of Section 16 "to make rules necessary or appropriate to carry out the provisions of this act" empowered the Commission to take such regulatory action and to "rule adversely upon rate and certificate filings without granting a hearing of the kind specified in Sections 4, 5 and 7". In other words, that everything which the Act authorizes the Commission to do after a hearing, it can determine or accomplish by general rule without a hearing and without findings, which rule it can apply to individual rates and applications also without hearing, without record and without findings of the statutory standards.

This is not an academic question. While here pointed to the Federal Power Commission, it transcends the Natural Gas Act and the particular issues here. It is a fundamental issue involving the power of all administrative agencies in our system of law: is such an agency the creature of its enabling statute and governed by the Congressional grants and limitations therein set out, or being once created is it beyond the control of such creator? Do regulated parties

have an opportunity to present the facts respecting a particular situation and to cross-examine and combat opposing allegations related thereto, or may they be precluded therefrom by general administrative rule promulgated without evidentiary support and founded on standards not provided to be applicable to the regulatory determination. If this Order may be sustained, may not the Commission by further general order, without any evidentiary hearing, determine that applications or rate schedules which depend on contracts providing for a price of more than 5¢ per mcf, or provide for *any* change in price during the term of the contract shall be rejected as contrary to public interest and creating an administrative burden on the regulatory body.

The decisions which upheld the constitutionality of the Act were based on the right to hearings provided therein. "The first prerequisite to an order by the Commission is that it shall be preceded by a hearing and findings." *FPC* v. *Natural Gas Pipeline Company of America* (1942) 315 U.S. 575, 583-584. If the position of the Ninth Circuit is correct in sustaining the statutory authority of the Commission to rule without hearing and findings, then the constitutionality of the Act itself will again be placed in issue as denying due process of law and the equal protection of the law.

The Court below held that there is no limit upon the power of an administrative agency to "fill in the interstices" of the enabling act except the agency's own concept of "the public interest". Further, that such interstitial legislation by the agency has all of the force of law and may without restriction affect the substantial rights of the regulated parties.

The Court below held that no hearing or record was necessary to support either a general rule or the specific

order applying such general rule to a rate or certificate determination. That Court went outside the record certified to it and held the Commission to be supported by evidence and findings in a totally foreign proceeding[5] to which Superior was not a party.

The Commission action was arbitrary and unreasonable. The Commission requires long term (20 years plus) contracts to assure the gas supply to the purchaser pipelines. This in turn requires the contracting parties to agree to some flexibility in the pricing provisions of their sale to take care of economic changes and conditions they cannot forsee. The Commission would prohibit this and now predict, at the producers' (not the Commission's) risk, what such conditions and the needs of the producers will be for 20 years. It is said that favored nation filings bear no apparent relationship to the economic requirements of the producers who file them. This ignores the internal competitive nature of the oil industry. If Company A is getting twice as much for its gas in an area as Company B, in competing for further leases in that area Company A has a definite advantage. First it has more ready cash; second, the landowners will tend to favor A, particularly if they have lands leased to both, when the disparity of royalty payment per unit of s sold is known. Further, suppose Companies A and B are seeking further capital. Obviously, B cannot compete with A in the money market.

Next the Commission said that such clauses have caused administrative burdens. How much greater is the administrative burden going to be if a producer, in order to avoid the danger of economic changes caused by inflation, or higher labor and materials, or more expensive operations,

[5] In the Matter of The Pure Oil Company, Docket No. G-17930, Opn 341, 25 FPC 383.

contracts for semi annual or annual rate increases, permitted by Order 242, instead of the conventional five-year escalation periods which they now accept as reasonably protective if accompanied by favored-nation and redetermination-of-price-at-reasonable-periods clauses. The hearing burden will be enlarged rather than reduced. Thus the rule here does not reasonably attain even its announced purpose.

CONCLUSION

For the foregoing reasons it is respectfully submitted that this petition for writ of certiorari should be granted.

Respectfully submitted,

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December 1963

APPENDIX A

UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

THE SUPERIOR OIL COMPANY,
Petitioner,
vs.
FEDERAL POWER COMMISSION,
Respondent.

No. 18,252
August 26, 1963,
as Amended
by Order of
Sept. 25, 1963

On Petition to Review Order of
The Federal Power Commission

Before: POPE, HAMLEY and BROWNING, Circuit Judges

HAMLEY, Circuit Judge:

This is a proceeding to review the action of the Federal Power Commission in rejecting, without hearing, certain rate-schedule and certificate-application filings. The filings had been tendered by petitioner, The Superior Oil Company (Superior). Superior is an independent producer of natural gas and is subject to Commission regulation under the Natural Gas Act (Act) 15 U.S.C. § 717. *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672.

On April 9, 1962, Superior entered into a casinhead gas contract with the El Paso Natural Gas Company (El Paso) covering the sale of casinghead gas produced in approximately 2,640 acres of gas in the Aneth Field in southeastern Utah. This contract incorporates by reference the terms

of a twenty-year casinghead gas contract entered into on June 11, 1958, by the same parties. This 1958 contract initially committed some 8,720 acres in the Aneth Field to El Paso,[1] but by subsequent agreements sections of 800 acres[2] and 2,560 acres[3] had been added to the contract. Nothing in the 1958 contract, which was in form amended by the 1962 contract, required or expressly permitted Superior to add acreage to that originally listed.

Among the terms incorporated in the 1962 contract by reference to the 1958 contract were certain price escalation clauses. One of these, not objected to by the Commission, called for specified price increases at five-year intervals.[4] Another provided for a price "redetermination" by the con-

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[1] On June 25 and July 7, 1958, Superior filed this 1958 contract with the Commission as its rate schedule No. 77, and in support of its application for a certificate of public convenience and necessity. Temporary authority to deliver this gas was granted by the Commission on November 18, 1958. On February 23, 1960, the Commission issued its Opinion No. 335, granting the certificate of public convenience and necessity applied for, but upon condition that the rate should be 17.7 cents per Mcf instead of 20 cents per Mcf, as proposed by Superior. *Superior Oil Co.*, 23 F.P.C. 370, *aff'd sub. nom., Texaco Inc.* v. *Federal Power Comm'n*, 5 Cir., 290 F. 2d 149. In order to comply with the order, Superior filed its supplement No. 7 to rate schedule No. 77, reducing the initial price to 17.7 cents. This supplement was accepted by the Commission on September 22, 1961.

[2] On February 17, 1960, Superior filed its second supplement to its original application and its supplement No. 4 to its rate schedule No. 77, to which was attached a supplemental casinghead gas contract between Superior and El Paso, dated December 30, 1959. Temporary authority to deliver from this additional 800 acres was granted by the Commission on May 19, 1960, such grant being modified on June 29, 1960.

[3] On June 7, 1960 Superior and El Paso entered into a second supplemental casinghead gas contract under which the original contract was amended and supplemented by the addition of approximately 2,560 acres of land to that previously covered. On July 20, 1960, Superior filed this supplemental contract as part

tracting parties, if requested by the seller, at each of these five year intervals.[5] A third escalation provision was a so-called favored-nation clause, wherein El Paso agreed that it would never pay Superior less than the

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of its supplement No. 5 to rate schedule No. 77, and its third supplement to the application for a certificate. Temporary authority to deliver this additional gas was granted by the Commission on September 21, 1960.

An additional supplemental casinghead gas contract, entered into between Superior and El Paso on January 1, 1961, the filings on which were accepted by the Commission on February 6, 1961, resulted in the deletion from the lands covered by the original contract of approximately 1,040 acres as to which title had been lost by litigation.

[4] The pricing terms of the original 1958 contract, adopted for the new acreage by the 1962 agreement called for an initial price of 20 cents per Mcf for the first five years commencing with the date of initial deivery under the original contract. It provided for a price of 21 cents per Mcf for the second five-year period, 22 cents per Mcf for the third five-year period, 23 cents per Mcf for the fourth five-year period, and 24 cents per Mcf thereafter if the contract remained in effect. The initial price was reduced to 17.7 cents per Mcf, in accordance with the condition attached to the certificate issued by the Commission for sale under the 1958 contract, as stated in note 1.

[5] The price redetermination clause provides specifically:

> "Seller shall have the right, at its option, to request a redetermination of the price provided in Section 7 of this Article to be paid for any one or more or all (but not part) of the periods set out in (b), (c), (d) and (e) above. Any such request made with respect to any of such periods shall be made in writing during the six (6) months immediately preceding the commencement of such period. If Seller shall make any such request, representatives of Buyer and Seller shall promptly meet and attempt to determine the then reasonable market price of the gas deliverable hereunder. In making such determination, consideration shall be given to all pertinent factors. The price so determined by Buyer and Seller shall be the price applicable during the entire period with respect to which the same was determined; provided, that if such price shall be less than the price provided in Section 7 of this Article with respect to such period, the price during such period shall be as provided in Section 7."

prices it was paying "others for comparable gas delivered under comparable conditions" within a specified area.[6]

On May 25, 1962, Superior applied to the Commission for an amendment to its certificate of public convenience and necessity for the purpose of authorizing it to sell gas to El Paso pursuant to the 1962 agreement. At the same time Superior made the related rate filing which would make the rate schedules then in effect, including the existing price escalation clauses described above, applicable to gas sold from the additional acreage.[7]

By letter-order dated June 15, 1962, the Commission summarily rejected, without hearing, the May 25, 1962 filings. In this order it was recited that the supplemental agreement of April 9, 1962, in effect incorporates by reference the terms of the contract of June 11, 1958, and therefore appears to incorporate pricing provisions other than those permitted by section 154.93 of the Commission's Regulations (18 C.F.R. [Cum. Supp. 1963] § 154.93).[8] Therefore, the Com-

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[6] The favored-nation clause provides:

> "Buyer agrees that the price to be paid from time to time to Seller hereunder for Residue Gas shall never be less than the price being paid by Buyer to others for comparable gas delivered under comparable conditions within the area shown on Exhibit 'B' attached hereto."

[7] This latter filing was denominated Superior supplement No. 8 to its gas rate schedule No. 77.

[8] Section 154.93 of the regulations, entitled "Rate schedule defined," provides in part:

> "*Provided,* That in contracts executed on or after April 3, 1962, for the sale or transportation of natural gas subject to the jurisdiction of the Commission, any provision for a change of price other than the following provisions shall be inoperative and of no effect at law; the permissible provisions for a change in price are:
>
> (a) Provisions that change a price in order to reimburse the seller for all or any part of the changes in production, severance, or gathering taxes levied upon the seller;

mission stated in this order, the proposed rate schedule supplement and related petition to amend, were rejected "in accordance with Commission Order No. 242 . . . and section 154.100 of the Commission's Regulations. . . ." See 18 C.F.R. § 154.100.[9]

(b) Provisions that change a price to a specific amount at a definite date; and

(c) Provisions that, once in five-year contract periods during which there is no provision for a change in price to a specific amount (paragraph (b) of this section), change a price at a definite date by a price-redetermination based upon and not higher than a producer rate or producer rates which are subject to the jurisdiction of the Commission, are not in issue in suspension or certificate proceedings, and, are in the area of the price in question; *Provided further*, That any contract executed on or after April 2, 1962, containing price-changing provisions other than the permissible provisions set forth in the proviso next above shall be rejected."

[9] Order No. 242, 27 F.P.C. 339, issued on February 8, 1962, promulgated the last-quoted proviso of section 154.93, and amended two other sections of the Commission's regulations, as follows (27 F.P.C. at 341):

"§ 157.14(a)(10) *Exhibit H — Total Gas Supply Data* (v), is amended by adding a proviso at the end thereof to read:

"*Provided, further, however*, That any contract executed on and after April 2, 1962, and filed in support of an applicant's gas supply showing will be given no consideration in determining adequacy of gas supply if it contains any price-changing provisions other than those defined as permissible in § 154.93 hereof."

"§ 157.25 *Necessary Exhibits, Exhibit R, Contracts*, is amended by deleting all the language after the first sentence thereof, ending with the words 'Natural Gas Act',' and inserting in lieu thereof the following:

"On or after April 2, 1962, the application shall be rejected if any contract submitted in support thereof contains any price-changing provisions other than those defined as permissible in § 154.93 hereof."

Section 154.100 of the Commission's regulations reads:

"The Commission reserves the right to reject any rate schedule or material submitted for filing which fails to comply with the requirements of §§ 154.92 through 154.99."

On July 9, 1962, Superior filed an application for reconsideration of the rejected supplement to the rate schedule, complaining that the summary rejection of its certificate application and related rate schedule filing was invalid. Superior did not contend that its contract did not contain price-changing provisions proscribed by the regulations relied upon by the Commission. Nor did the company make any request for an amendment of the regulation in question which would render it inapplicable as to price-changing clauses of the kind here involved, or for a waiver of the regulation as to this sale.[10]

Since the Commission did not act on the application for reconsideration, it was denied by operation of law on August 8, 1962.[11] This petition for review followed.

Under the existing regulations, referred to above, there being no request for an amendment, waiver or repeal thereof, and no contention that the rejected filings did not contain price-changing provisions proscribed thereunder, the Commission was required to summarily reject the filings without hearing. It follows that the only real issue presented on this review is the validity of the regulations pursuaunt to which summary rejection was ordered.

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[10] At this time, the Commission's Rule § 1.7(b), 12 Fed. Reg. 8473 (1947), expressly provided procedures whereby interested persons could seek amendment or repeal of rules. There was then no express provision with regard to obtaining waiver of a Commission rule. In our opinion, however, such a procedure was then implicitly provided for by § 1.7-(a) of the Commission rules. This subsection provides generally for "(p)etitions for relief under any statute or other authority delegated to the Commission. . . ." Our view as to this accords with that expressed by the Commission on September 20, 1962, in explaining an amendment to § 1.7(b), adopted at that time, wherein express reference to "waiver" relief was first incorporated into the rule. See Order No. 255, Docket No. R-222, 27 Fed. Reg. 9499 (1962). Rule § 1.7(b) was again amended on November 6, 1962. See Order No. 255, amended, Docket No. R-222, 27 Fed. Reg. 11001 (1962).

[11] See section 19(a) of the Act, 15 U.S.C. § 717r.

As a basis for discussing Superior's attack upon these regulations it will be helpful to set out in detail their procedural history.

They had their inception in rule-making proceedings instituted in 1956. In the notice of this proposed rule-making, the Commission stated that it proposed to amend section 154.93 of its General Rules and Regulations (18 C.F.R. §154.93) relating to the filing of rate schedules by independent producers, to describe certain types of contracts for the sale of natural gas which would not be accepted for filing as rate schedules.

The Commission's specific proposal was that it would not accept for filing contracts containing provisions calling for price adjustments stemming from:

> "(a) escalation clauses based on price indices or changes in the price received by the purchaser upon resale, or (b) the payment or offer of payment of higher prices by the purchaser or other purchasers in the same or other producing areas to the same or other sellers."

21 Fed. Reg. 2389 (1956)

The Commission, in its notice, invited comments on or before June 1, 1956, and stated that it would not act prior to that date. Numerous responses were received by the Commission, including a protest from Superior. No further public action was taken in this rule-making proceeding until March, 1961. The record does not disclose the reason for the delay.

On March 3, 1961, *Pure Oil Co.*, 25 F.P.C. 383, was decided in which it was held, among other things, that, for a number of stated reasons, the two-party favored-nation clauses in Pure Oil Company's contract with El Paso, and

indefinite escalation clauses generally, are contrary to the public interest.[12]

In its *Pure Oil* decision the Commission concluded that it could not strike, as void or voidable, such clauses from Pure Oil Company's existing contracts. But the Commission announced its purpose to deal with the problem by issuing, for future application, regulations in appropriate Commission proceedings, including the rule-making proceedings which had been instituted in 1956.

In keeping with this announcement in the *Pure Oil* decision, the Commission on March 3, 1961, which was the day on which that decision was issued, filed its Order No. 232, in the rule-making proceeding (25 F.P.C. 379). After reciting the history of the rule-making proceeding, the Commission made certain general findings followed by several decretal provisions. These provisions added to the definitions contained in section 154.91(a) of the Commission's General Rules and Regulations (18 C.F.R. § 154.91(a)), definitions of the terms "definite escalation clause," and "indefinite escalation clause," and added a proviso at the end of section 154.93, *Rate schedule defined*. The result was to declare inoperative, and of no effect at law, indefinite escalation clauses, as defined, contained in contracts tendered for filing on and after April 3, 1961.

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[12] This Commission decision was affirmed. *Pure Oil Co.* v. *Federal Power Comm'n*, 7 Cir., 299 F. 2d 370. Indefinite escalation clauses generally include, in addition to two-party favored-nation clauses of the kind included in the Pure Oil Company contract, three-party favored-nation clauses, periodic escalation clauses, redetermination clauses, spiral escalation clauses, and other similar types of clauses. These various kinds of clauses are defined in *Pure Oil Co.*, 25 F.P.C. 383, 388, note 3.

Order No. 232 provided that any interested party might submit to the Commission, on or before March 20, 1961, views or comments in writing concerning these rule amendments. Interested persons did submit views and comments in response to this invitation, although none were filed by Superior. On March 31, 1961, upon consideration of these comments, and upon its own further consideration, the Commission issued its Order No. 232 A, modifying the amendments promulgated by Order No. 232 (25 F.P.C. 609).

In Order No. 232 A, the Commission reaffirmed the findings contained in its Order No. 232, that the use of long-term contracts for the sale of natural gas by producers to pipelines or to others is desirable and appropriate in the public interest but that indefinite escalation provisions are, in general, contrary to the public interest. The Commission stated, however, that it appears that elimination of all indefinite escalation provisions, as accomplished by Order No. 232, would be too restrictive to enable the industry adequately to cope with possible changing economic conditions over the span of long-term contracts. The Commission therefore concluded that, to allow for pricing flexibility and to provide an incentive for long-term contracts, it should permit future contracts to contain limited price redetermination provisions, invocable not more than once in every five-year contract period and based upon rates subject to the Commission's jurisdiction.

Giving effect to this change of view, the Commission amended the findings contained in Order No. 232 pertaining to indefinite escalation clauses and the need of regulations governing such clauses. It also withdrew from section 154.91(a) the definitions of "definite escalation clause," and "indefinite escalation clause," which Order No. 232 had added to its regulations, and amended the proviso which

that order had added to section 154.93, *Rate schedule defined*, to read in pertinent part as set out in the margin.[13]

The result was that, effective as to contracts for the sale or transportation of natural gas executed on or after April 3, 1961, all price changing provisions were determined in advance to be inoperative and of no effect at law, except those falling within the three numbered clauses specified in the proviso, quoted in note 13.[14]

On October 10, 1961, the Commission initiated new rulemaking proceedings. In its notice to interested persons,

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[13] "*Provided*, That in contracts executed on or after April 3, 1961, for the sale or transportation of natural gas subject to the jurisdiction of the Commission, any provision for a change of price other than the following provisions shall be inoperative and of no effect at law; the permissible provisions for a change in price are:

"(1) provisions that change a price in order to reimburse the seller for all or any part of the changes in production, severance, or gathering taxes levied upon the seller;

"(2) provisions that change a price to a specific amount at a definite date; and

"(3) provisions that, once in five-year contract periods during which there is no provision for a change in price to a specific amount [paragraph (2)], change a price at a definite date by a price-redetermination based upon and not higher than a producer rate or producer rates which are subject to the jurisdiction of the Commission, and not in issue in suspension or certificate proceedings, and are in the area of the price in question."

[14] Sun Oil Company thereafter filed with the Commission an application for a rehearing with regard to Orders Nos. 232 and 232 A. The application was rejected by the Commission and Sun Oil Company filed a petition for review in the Fifth Circuit Court of Appeals. That court dismissed the application, holding that Orders Nos. 232 and 232 A are not determinative of status, do not adjudge rights or obligations nor direct the taking or refraining from any particular action, and are therefore not subject to review under the Act. *Sun Oil Co. v. Federal Power Comm'n*, 5 Cir., 304 F. 2d 293, 294, *cert. denied*, 371 U.S. 861.

including natural gas companies, the Commission noted the amendment of section 154.93 of its regulations accomplished by Order 232 A, and then stated:

> "Having found in Order No. 232 A that indefinite escalation provisions . . . are generally undesirable, unnecessary and incompatible with the public interest for the due and proper development of natural gas service by natural gas companies . . . it appears that no useful purpose can be served by the Commission's acceptance of contracts containing indefinite price escalation provisions or of applications relying upon contracts having such provisions as proof of the applicants' gas supply.

26 Fed. Reg. 9732, 1961.

The specific amendments proposed, as set out in this notice were substantially the same as those eventually adopted in Order No. 242, described below. The Commission, in its notice, invited comments on or before November 13, 1961. Numerous responses were received, both in support of, and in opposition to, the proposed amendments. Superior filed a timely comment in which it took the position that the proposed amendments are unlawful and exceed the powers granted to the Commission under the Act; contrary to the public interest; unnecessary; prematurely proposed; and arbitrary, unreasonable and discriminatory.

In this rule-making proceeding the Commission, on February 8, 1962, issued Order No. 242 (27 F.P.C. 339). In that order the Commission promulgated certain amendments to its regulations providing for: (1) the rejection of contracts containing indefinite price escalation clauses (now called "price-changing provisions") of the kind outlined in Order No. 232 A, (2) the rejection of applications for certificates of public convenience and necessity rely-

ing for a gas supply upon contracts containing such indefinite escalation provisions, and (3) the Commission's refusal to consider such contracts submitted in support of certificate applications by pipeline companies.[15]

In promulgating these amendments the Commission purported to act pursuant to authority granted by the Act, and particularly sections 4, 5, 7 and 16 thereof, (15 U.S.C. §§ 717c, 717d, 717f and 717o). See 27 F.P.C. 339. In Order No. 242, the Commission indicated its adherence to the findings and conclusions contained in its *Pure Oil* decision, and in Order No. 232 A to the effect that indefinite escalation clauses are contrary to the public interest. The Commission also reemphasized the view, previously expressed in the *Pure Oil* decision and Order No. 232 A, that filings under such clauses have unreasonably burdened the Commission.[16]

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[15] These amendments were accomplished by amending, effective April 2, 1962, Parts 154 and 157, subchapter E, chapter I, of Title 18 of the Code of Federal Regulations, to add the last proviso now contained in section 154.93 (quoted in note 5 above), and to amend sections 157.14 (a)(10), and 157.25, as quoted in note 6 above.

[16] As to this the Commission said in Order No. 242:

> "Filings under indefinite escalation clauses have created a significant portion of the administrative burdens under which this Commission is laboring today. The Natural Gas Act contemplates that rate increases shall be sought when there is economic justification but not that there shall be a chain reaction in a wide area whenever one producer in the area negotiates a contract at a new price level. The act requires the Commission to give precedence to the hearing and decision of rate increases, but the complexity of indefinite price clauses requires it to spend an undue amount of time in their interpretation and application at the expense of making a prompt determination of the rate issues involved. Accordingly, in protecting the public against waves of increases which have no defensible basis, we also serve the need — which we believe we should take into account — of making the tasks of regulation more manageable."

A number of producers, including Superior, filed applications for rehearing of Order No. 242. These were denied on April 4, 1962 (27 F.P.C. 666).[17]

Having set out the procedural history of the Commission regulations pursuant to which the Commission summarily rejected the filings in question, we now turn to a discussion of the arguments advanced by Superior in attacking the validity of those regulations.

Superior contends that the amended form of section 154.93 of the regulations, upon which the Commission relied in rejecting Superior's filings, is invalid because Superior was not accorded an evidentiary hearing in connection with the issuance of Order No. 242, which promulgated the critical amendment to that regulation.[18] Superior urges that failure to grant such a hearing not only violates the Act, but also denies due process of law, as guaranteed by the Fifth Amendment.

The Act does not specify the procedures to be followed by the Commission in prescribing or amending rules and regulations, but provides only the general authority to prescribe, issue, make, amend and rescind them. See section 16 of the

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[17] Six petitions for review of that order were thereafter filed. In each case the Commission moved to dismiss on the ground that the order was not reviewable prior to a specific application. Responsive to such motions one of these petitions for review was dismissed by the Third Circuit on July 17, 1962. *Shell Oil Co.* v. *Federal Power Comm'n* (not reported). Three of these petitions were dismissed by the Fifth Circuit on August 14, 1962. *Hunt Oil Co.* v. *Federal Power Comm'n*, 5 Cir., 306 F.2d 878. The remaining two petitions were dismissed by the Tenth Circuit on May 20, 1963. *Pan American Petroleum Corp.* v. *Federal Power Comm'n*, 10 Cir., 317 F.2d 796.

[18] This was the addition of the final proviso, reading:

"*Provided further*, That any contract executed on or after April 2, 1962, containing price-changing provisions other than the permissible provisions set forth in the proviso next above shall be rejected."

27 F.P.C. at 340.

Act, 15 U.S.C. § 717o. The procedures to be followed in prescribing or amending administrative rules and regulations, including those of the Commission, are dealt with in section 4 of the Administrative Procedure Act, 5 U.S.C. § 1003, to which Superior makes no reference. The procedures followed by the Commission which led to the issuance of Order No. 242, amending section 154.93 of the regulations, as described above, comport fully with the requirements of that statute.

In legislation, or rule-making, there is no constitutional right to any hearing whatsoever. *Bowles* v. *Willingham*, 321 U.S. 503, 519; *Willapoint Oysters, Inc.* v. *Ewing*, 9 Cir., 174 F. 2d 676, 694, *cert. denied*, 338 U.S. 860.

Superior contends that section 154.93 of the regulations, and section 154.100, as applied here, are invalid, because, assuming that the Commission has substantive authority to reject such contract provisions (a proposition which Superior denies and which will be discussed below), such authority must stem from sections 4, 5 and 7 of the Act, 15 U.S.C. §§ 717c, 717d and 717f, each of which requires the Commission to act only after hearing, and no hearing was accorded Superior.

Superior's amendment to its certificate application, filed May 25, 1962, for the purpose of including therein Superior's interest in the 2,690 additional acres of gas dedicated to El Paso by the contract of April 9, 1962, was filed pursuant to section 7c of the Act, 15 U.S.C. § 717f(c).

Under that section, with exceptions not here relevant, no natural gas company may engage in the transportation or sale of natural gas, or undertake the construction or extension of any facilities therefor, or acquire or operate any such facilities or extensions thereof, unless there is in force with respect to such company a certificate of public con-

venience and necessity issued by the Commission authorizing such acts or operations. This section further provides that, except in the case of so-called "grandfather" rights, or temporary certificates, the Commission shall set any application for such a certificate for hearing, the application to be decided, and the certificate to be issued or denied according to the procedure provided in section 7(e) of the Act 15 U.S.C. § 717b(e). Section 7(e) specifies the standards to be applied in determining whether a certificate should issue and provides that the Commission may attach reasonable terms and conditions.[19]

Superior's notice of change in rate schedule No. 77 (supplement No. 8), was also filed on May 25, 1962. This was done, as heretofore stated, pursuant to section 4(d) of the Act, 15 U.S.C. § 717c(d), and for the purpose of applying, to the newly-dedicated acreage, the existing rates and contract rate provisions then in effect between Superior and El Paso. Under section 4(e) of the Act, 15 U.S.C. § 717c(e), the Commission is given authority to enter upon a hearing concerning the lawfulness of rates, charges, classifications, or service described in a section 4(d) filing, and, after full hearings, may make such orders with reference thereto as

[19] "(e) Except in the cases governed by the provisos contained in subsection (c) of this section, a certificate shall be issued to any qualified applicant therefor, authorizing the whole or any part of the operation, sales, service, construction, extension, or acquisition covered by the application, if it is found that the applicant is able and willing properly to do the acts and to perform the service proposed and to conform to the provisions of this chapter and the requirements, rules, and regulations of the Commission thereunder, and that the proposed service, sale, operation, construction extension, or acquisition, to the extent authorized by the certificate, is or will be required by the present or future public convenience and necessity; otherwise such application shall be denied. The Commission shall have the power to attach to the issuance of the certificate and to the exercise of the rights granted thereunder such reasonable terms and conditions as the public convenience and necessity may require."

would be proper in a proceeding initiated after it had become effective. The authority of the Commission to issue orders with regard to rates, charges, classifications, or services already, in effect, and providing for hearings, is set out in section 5(a) of the Act, 15 U.S.C. § 717d(a).

Superior represents that, if given an opportunity at a hearing, it would show that the particular price-changing clauses contained in its contract with El Paso have a definite relation to the economic requirements of Superior and to the economic conditions of the country and of the industry. It would further show, the company asserts, that the circumstances of Superior's operations in general and in the Aneth Field not only justify but require this type of indefinite pricing provision if there is to be any relation between the price for which Superior files in the future and the economic conditions then existing, and the economic requirements of Superior. Its evidence would conclusively demonstrate, Superior states, that the particular types of flexible pricing provisions used in its contracts are much more closely related to economic conditions and requirements than are the price provisions permitted under Order No. 242.

The substantive authority of the Commission to change contracts, if it exists at all,[20] stems from sections 4, 5 and 7 of the Act, as the Commission concedes. Those sections, as the text quoted above indicates, require that in proceedings involving particular rate and certificate filings, had for the purpose of exercising those substantive rights, a hearing must be accorded. But the precise question here is whether the Commission is limited, in the exercise of this substantive authority, to *ad hoc* proceedings under sections 4, 5 and 7, wherein hearings are concededly required, or whether it

[20] To be discussed below.

may, at least to the extent represented by the specific regulations here involved, exercise that substantive authority pursuant to its rule-making authority under section 16 of the Act, 15 U.S.C. § 717o.[21]

The specific regulations here invoked are those under which price redetermination clauses and favored-nation clauses of the kind contained in the Superior-El Paso contract,[22] were determined in advance to be contrary to the public interest and filings containing them were made subject to summary rejection without hearing. We are not here concerned with the validity of those regulations insofar as they may affect price-changing clauses of a kind not involved in this proceeding.[23]

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[21] Section 16 reads, in pertinent part:

"The Commission shall have power to perform any and all acts, and to prescribe, issue, make, amend, and rescind such orders, rules, and regulations as it may find necessary or appropriate to carry out the provisions of this chapter. Among other things, such rules and regulations may define accounting, technical, and trade terms used in this chapter; and may prescribe the form or forms of all statements, declarations, applications, and reports to be filed with the Commission, the information which they shall contain, and the time within which they shall be filed. . . . For the purposes of its rules and regulations, the Commission may classify persons and matters within its jurisdiction and prescribe different requirements for different classes of persons or matters. All rules and regulations of the Commission shall be filed with its secretary and shall be kept open in convenient form for public inspection and examination during reasonable business hours. June 21, 1938, c. 556, § 16, 52 Stat. 830."

[22] See notes 5 and 6.

[23] The desirability of confining this question to the specific price-changing clauses here in question is demonstrated by what has happened in another proceeding pending before the Commission. In *Atlantic Ref. Co.*, F.P.C. Docket No. CI 63-576, the Commission, on February 21, 1963, granted a rehearing to consider whether the regulations here invoked should be modified to permit escalation clauses in producer contracts which allow producers to change the price under a particular contract at will.

In our opinion *United States* v. *Storer Broadcasting Co.*, 351 U.S. 192, requires us to hold that to the extent here exercised, and assuming existence of substantive authority, the Commission had power to provide by rule for summary rejection of rate and certificate filings, and was not required to exercise such authority through the medium of *ad hoc* proceedings under sections 4, 5 and 7, wherein hearings would have been required.

Storer involved the Communications Act of 1934, as amended, 47 U.S.C. § 301 et seq. Prior to November, 1953, Storer Broadcasting Co. owned or controlled five television broadcast stations. Proceeding under section 308 of the Communications Act, 47 U.S.C. § 308, the company applied to that Commission for a license to operate a sixth television station at Miami, Florida.

On November 25, 1953, while that application was pending, that Commission, exercising its rule-making power under sections 4(i) and 303(f) and (r), 47 U.S.C. §§ 154(i), 313(f) and (r) of the Communications Act, amended its Rule § 3.636 with regard to multiple ownership of television broadcasting stations. Under the rule, as amended, it was provided, among other things, that no license for a television broadcast station shall be granted to any party who owns any other television broadcasting station "if the grant of such license would result in a concentration of control of television broadcasting in a manner inconsistent with public interest, convenience, or necessity." (351 U.S. at 194, n. 1) The amended form of the rule also contained a provision declaring that ownership or control of more than five television broadcasting stations would be considered to be a "concentration of control contrary to the public interest, convenience or necessity."[24] (Id.)

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[24] The Communications Commission's Rules 1.361(c) and 1.702 permit applicants to seek amendments and waivers of or exception to its rules. See 351 U.S. at 201, n. 10.

On the day this rule amendment was promulgated, the Federal Communications Commission, on the basis of the amended rule dismissed, without hearing, Storer's pending application for a sixth television station at Miami.

Storer sought a review, in the Court of Appeals for the District of Columbia, of the order promulgating the rule amendment pursuant to which its application was denied. It contended that this rule, as amended, was in conflict with the statutory mandates that applicants should be granted licenses if the public interest would be served and that applicants must have a hearing before denial of an application. The statutory provisions relied upon by the company were sections 309(a) and (b) of the Communications Act, as they existed prior to 1960.[25]

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[25] Sections 309(a) and (b), 47 U.S.C. § 309(a) and (b) which have undergone amendment since 1955 then read (351 U.S. at 195, n. 5):

> "(a) If upon examination of any application provided for in section 308 of this title the Commission shall find that public interest, convenience, and necessity would be served by the granting thereof, it shall grant such application."
>
> "(b) If upon examination of any such application the Commission is unable to make the finding specified in subsection (a) of this section, it shall forthwith notify the applicant and other known parties in interest of the grounds and reasons for its inability to make such finding. . . . Following such notice, the applicant shall be given an opportunity to reply. If the Commission, after considering such reply, shall be unable to make the finding specified in subsection (a) of this section, it shall formally designate the application for hearing on the grounds or reasons then obtaining and shall notify the applicant . . . specifying with particularity the matters and things in issue. . . . Any hearing subsequently held upon such application shall be a full hearing in which the applicant and all other parties in interest shall be permitted to participate but in which both the burden of proceeding with the introduction of evidence upon the issue specified by the Commission, as well as the burden of proof upon all such issues, shall be upon the applicant."

The Court of Appeals struck out, as contrary to §§ 309(a) and (b), as they then existed, the provision added to Rule § 3.636 declaring that ownership or control of more than five television broadcasting stations would be considered to be a concentration of control contrary to the public interest, convenience or necessity (*Storer Broadcasting Co.* v. *United States*, D.C. Cir., 220 F.2d 204).

The Supreme Court reversed, holding that the hearing requirement of then section 309(b) did not withdraw from the power of the Communications Commission the authority, under its rule-making power, to promulgate the provision limiting applicants to five television broadcasting stations. The Supreme Court recognized that the challenged rule contained limitations against licensing not specifically authorized by statute. However, such general rule-making power, the Court held, is not limited to specific authorizations, but extends to matters not inconsistent with the Communications Act or law.

The Supreme Court further stated, in *Storer* (pages 203-205):

> "This Commission, like other agencies, deals with the public interest. *Scripps-Howard Radio* v. *Federal Communications Comm'n*, 316 U.S. 4, 14. Its authority covers new and rapidly developing fields. Congress sought to create regulations for public protection with careful provision to assure fair opportunity for open competition in the use of broadcasting facilities. Accordingly, we cannot interpret § 309(b) as barring rules that declare a present intent to limit the number of stations consistent with a permissible 'concentration of control.' It is but a rule that announces the Commission's attitude on public protection against such concentration. The Communications Act must be read as a whole and with appreciation of the responsibilities of the body charged with its fair and efficient operation.

The growing complexity of our economy induced the Congress to place regulation of businesses like communication in specialized agencies with broad powers. Courts are slow to interfere with their conclusions when reconcilable with statutory directions. We think Multiple Ownership Rules, as adopted, are reconcilable with the Communications Act as a whole. An applicant files his application with knowledge of the Commission's attitude toward concentration of control.

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"... We read the Act and Regulations as providing a 'full hearing' for applicants who have reached the existing limit of stations, upon their presentation of applications conforming to Rules 1.361(c) and 1.702, that set out adequate reasons why the Rules should be waived or amended. The Act, considered as a whole, requires no more. We agree with the contention of the Commission that a full hearing, such as is required by § 309(b), n. 5, *supra*, would not be necessary on all such applications. As the Commission has promulgated its Rules after extensive administrative hearings, it is necessary for the accompanying papers to set forth reasons, sufficient if true, to justify a change or waiver of the Rules. We do not think Congress intended the Commission to waste time on applications that do not state a valid basis for a hearing. If any applicant is aggrieved by a refusal, the way for review is open." (Footnotes omitted.)

There is no substantial difference between the statutes involved in *Storer* and those involved in the case before us, insofar as hearing requirements and rule-making authority are concerned. As in the case of the rules of the Federal Communications Commission, the Federal Power Commission regulations permit applicants to seek amendment,

waiver or repeal of its rules.[26] In *Storer*, as well as here, the effect of the rule, as applied, was to occasion summary denial of the application without hearing.[27] In *Storer* as well as here, the rule under attack represented an exercise of substantive authority.[28] Indeed, it was only because the rule there challenged was found to affect Storer's substantive rights that the Supreme Court held that the company had standing to petition for review of that rule.

Seeking to distinguish *Storer*, Superior points out that section 314 of the Communications Act of 1934, 47 U.S.C. § 314, expressly forbids ownership or control of stations where the purpose or the effect thereof might be to substantially lessen competition or to restrain commerce. It

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[26] As pointed out in footnote 10, the Federal Power Commission's Rules in effect at that time provided expressly for the amendment or repeal of rules, and implicitly for their waiver. The Federal Communications Commission's rules in effect at the time *Storer* was decided, provided expressly for amendment, repeal or waiver of that Commission's rules. See *United States* v. *Storer Broadcasting Co.*, 351 U.S. 192, 202-203, note 10.

[27] In *Storer*, the application which was so denied was pending when the rule amendment was promulgated, whereas here, the filings in question were not pending, nor had the supplemental contract upon which they were based been executed when Order No. 242 was issued on February 8, 1962.

[28] In *Storer* the Supreme Court observed (pages 199-200):

"The regulations here under consideration presently aggrieve the respondent. The Commission exercised a power of rulemaking which controls broadcasters. The Rules now operate to control the business affairs of Storer. Unless it obtains a modification of this declared administrative policy, Storer cannot enlarge the number of its standard or FM stations. It seems, too, that the note to Rule 3.636 (n. 1, *supra*) endangers Storer's stations as alleged in its petition for review. See this opinion, *supra*, p. 197, at (b). Commission hearings are affected now by the Rules. Storer cannot cogently plan its present or future operations. It cannot plan to enlarge the number of its standard or FM stations, and at any moment the purchase of Storer's voting stock by some member of the public could endanger its existing structure. These are grievances presently restricting Storer's operations. . . ." (Footnotes omitted.)

is argued from this that the Communications Commission was clearly authorized to promulgate rules to further the Congressional directive expressed in the Act.

This argument, however, goes only to the question of whether the Commission has substantive authority to reject applications which contain the proscribed price-changing clauses, whether by *ad hoc* proceedings or by general rule making — a question to be explored below. The requirements of the Communications Act with respect to the necessity of hearings are just as firm as in the Natural Gas Act. If the Communications Act requirements did not foreclose substantive regulation by means of rule-making under the circumstances of *Storer*, we do not perceive why the Natural Gas Act requirements do so under the circumstances of this case.

Superior also notes that the Communications Act involves the use of the public domain and does not pertain to rate regulation, whereas the property rights of natural gas companies are being subjected to regulation under the rate and certificate provisions of the Natural Gas Act. Accordingly, Superior argues, under the Communications Act there can be no question of confiscation of private property protected by the Fifth Amendment, whereas under the Natural Gas Act, the protection against confiscation is clear.

But again, we are not at this point considering the constitutionality of the challenged Federal Power Commission regulation, but only its validity in view of the provisions of the Act relating to the necessity for hearings. Of course if the regulations in question are unconstitutional, a question to be considered below, they cannot stand whether or not in conflict with statutory provisions pertaining to hearings.

Superior cites a number of decisions which it believes support the view that the regulations in question violate

provisions of the Act relating to hearings.[29] None of these cases represented Commission action based upon a general rule, applied prospectively, in which the Commission had given concreteness to a standard of public interest. We have no doubt that, absent such a rule, or absent Commission action reasonably based thereon, the Commission may not rule adversely upon rate and certificate filings without granting a hearing of the kind specified in sections 4, 5 and 7. But that is not our case.

We are mindful of the fact that the Tenth Circuit has recently held Order No. 242 void and without effect. *Pan American Petroleum Corp.* v. *Federal Power Comm'n*, 10 Cir., 317 F. 2d 796, decided May 20, 1963.[30] That court appears to have reached this conclusion at least partly on the ground that Order No. 242 violates sections 4, 5 and 7 of the Act, in which hearings are provided for. Since, for the reasons indicated, we regard *Storer*, as controlling on the question of the statutory necessity for a hearing, we respectfully decline to follow the *Pan American* decision.

Superior argues that, apart from the hearing requirements of sections 4, 5 and 7 of the Act, the summary rejection of its rate and certificate filings denied it procedural due process of law guaranteed by the Fifth Amendment, since due process entitled it to a hearing.

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[29] Principal among these are *The Atlantic Refining Co.* v. *Public Service Comm'n* (Cateo), 360 U.S. 378; *United Gas Pipe Line Co.* v. *Memphis Light, Gas & Water Div.* (Memphis), 358 U.S. 103; *Federal Power Comm'n* v. *Natural Gas Pipeline Co.*, 315 U.S. 575; *Willmut Gas & Oil Co.* v. *Federal Power Commission*, D.C. Cir., 294 F.2d 245, *cert. denied*, 368 U.S. 975; and *Mississippi River Fuel Corp.* v. *Federal Power Comm'n*, 3 Cir., 202 F.2d 899, dismissed on motion of petitioner, 345 U.S. 988.

[30] The Tenth Circuit held that Orders Nos. 232 and 232 A are in a different category because they are only advisory declarations of Commission policy and determine no rights.

This constitutional question was not expressly raised in *Storer*. Nevertheless, it seems to us that decision, by implication, calls for rejection of Superior's argument. If the explicit amendment and repeal provisions and the implicit waiver provision of the agency's rules are sufficient to meet the requirements of the express statutory provisions pertaining to hearings (and we have held that they are), it would seem that they are also sufficient to meet the procedural requirements of the Due Process Clause of the Fifth Amendment.

Order No. 232 A brought about the rule amendment by means of which the Commission determined, for prospective application, that certain kinds of price-changing clauses are contrary to the public interest. The rule amendment thereby accomplished thus gave specificity, in a particular area, to the statutory standard of public interest. Assuming that the Commission had substantive authority to promulgate this amendment (to be inquired into below), the rule had the same function and effect as if it were a statute proscribing, in the same explicit terms, the described price-changing provisions. So viewed, and absent special circumstances that would have warranted a request for amendment, repeal or waiver thereof, the application in a particular case of the explicit standard stated therein no more entitled persons affected to an evidentiary hearing as to the general merit of the standard than would have been the case if this concreteness had been expressed in the statute itself.

That an evidentiary hearing would not have been necessary in the latter case is made clear in *Denver Union Stock Yard Co.* v. *Producers Livestock Marketing Association*, 356 U.S. 282. The court there pointed out that the need for an evidentiary hearing, present when it is proposed to apply a statute couched in general terms, does not exist where

the statute defines a duty in explicit terms.[31] For the reasons stated above, we regard this principle as applicable to the rule amendment accomplished by Order No. 232 A. The rule amendment effectuated by Order No. 242, providing for summary rejection of price-changing clauses proscribed under the rule promulgated by Order No. 232 A, also gave effect to this principle and, in our opinion, does not offend the Due Process Clause.

In contending that due process of law entitled it to an evidentiary hearing, Superior cites a number of decisions which we now notice.

The most recent of these is *Hannah* v. *Larche*, 363 U.S. 420, sustaining the validity of certain rules of procedure adopted by the Commission on Civil Rights. We find nothing in this opinion which supports petitioner's view. The court there held that since the Commission on Civil Rights makes no adjudication but acts solely as an investigative and fact-finding agency, the questioned rules of procedure under which affected persons were not afforded a hearing, do not violate the Due Process Clause.

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[31] In the *Denver Union Stockyard* case, the Court said, at page 287:

"When an Act condemns a practice that is 'unfair' or 'unreasonable,' evidence is normally necessary to determine whether a practice, rule, or regulation transcends the bounds. See *Associated Press* v. *Labor*, 301 U.S. 103; *Chicago Board of Trade* v. *United States*, 246 U.S. 231; *Sugar Institute* v. *United States*, 297 U.S. 553. But where an Act defines a duty in explicit terms, a hearing on the question of statutory construction is often all that is needed. See *Securities and Exchange Comm'n* v. *Ralston Purina Co.*, 346 U.S. 119 (public offering); *Addison* v. *Holly Hill Co.*, 322 U.S. 607 (area of production). It is, of course, true that § 310 of the Act provides for a 'full hearing' on a complaint against a 'regulation' of a stockyard. That was also true of the Act involved in *United States* v. *Storer Broadcasting Co.*, 351 U.S. 192. But we observed in that case that we never presume that Congress intended an agency 'to waste time on applications that do not state a valid basis for a hearing.' *Id.*, at 205."

In *Hannah* the Court pointed out that the requirements of due process frequently vary with the type of proceeding involved. Thus, said the Court, at page 442, in the passage which we assume Superior relies upon, when governmental agencies "adjudicate or make binding determinations which directly affect the legal rights of individuals, it is imperative that those agencies use the procedures which have traditionally been associated with the judicial process."

But the rules here under challenge are not adjudicatory in nature. They do not affect any contractual right which was in existence when the rule became effective. The problem would be different if the effect of the rules was to proscribe rates already in effect.[32] Moreover, under the Commission's rules, if there are any circumstances which indicate that the schedules or contracts in question do not contain proscribed clauses, or that the rules should be amended to except price-changing clauses of a particular kind, or waived in a particular case, the applicant is afforded a hearing.

Another case relied upon by Superior is *Morgan* v. *United States*, 304 U.S. 1. In this case, however, as was pointed out in *Hannah* (at page 451), the government agency made a determination in the nature of an adjudication affecting

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[32] In *Wisconsin* v. *Federal Power Comm'n*, 373 U.S. 294, the Court, commenting upon a contention by the State of California that the Commission should have declared void, *ab initio*, spiral escalation clauses in the contracts of Phillips Petroleum Co., referred to Commission Orders Nos. 232, 232 A and 242. In this connection the Court said, at page 304:

> "Further, we see no merit in California's contention. It is true that the Commission has announced *prospectively* that it would not accept for filing contracts containing such clauses, but it would have been quite a different matter for the Commission to have declared that *past* rate increases were ineffective simply because they were based on spiral provisions. . . ." (Footnote omitted.)

legal rights. What happened was that the Secretary of Agriculture fixed the maximum rates to be charged by market agencies at stockyards without conducting a trial-like hearing. This decision may or may not be authority for holding that the Commission cannot validly, by rule, proscribe escalation clauses which would allow producers to change the price under a particular contract at will, subject only to Commission regulations.[33] But the rules, as applied to the particular price-changing clauses involved here do not, in our opinion, partake in any degree of a maximum rate order, or a rate-freezing order, especially in view of the leeway allowed under the waiver provision to bring special circumstances to the attention of the agency.

The third Supreme Court decision relied upon by Superior in connection with the question under discussion is *Northern Pac. Ry. Co.* v. *Department of Public Works*, 268 U.S. 39. As in *Morgan*, however, the agency proceeding was one for the purpose of fixing rates. The Court held that in such a proceeding an order based upon a finding made without evidence or upon evidence which clearly does not support it, is a denial of due process. For the reasons stated in discussing *Morgan*, this decision is not in point here.

Only one of the remaining cases cited by Superior on this branch of the case warrants more than passing comment.[34] We refer to *Philadelphia Co.* v. *Securities & Exchange*

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[33] It has previously been noted that the Commission is now giving consideration to a modification of its rules to permit escalation clauses of this kind. See note 23 above.

[34] Thus *Warren Petroleum Corp.* v. *Federal Power Comm'n*, 10 Cir., 282 F. 2d 312, does not appear to involve any constitutional question. *National Labor Relations Bd.* v. *Burns*, 8 Cir., 207 F. 2d 437, involved an unfair labor practice proceeding, clearly adjudicatory in nature, in which the Examiner excluded competent and material evidence. *National Labor Relations Bd.* v. *Prettyman*, 6 Cir., 117 F. 2d 786, involved the same kind of proceeding.

Comm'n, D.C. Cir., 175 F. 2d 808, *dismissed as moot* 337 U.S. 901.

Pittsburgh Railways, then in process of reorganization, was a "non-utility subsidiary" of The Philadelphia Company, a registering holding company, and under an S.E.C. rule, exempt from regulation under that Act. That Commission issued notice of a proposed rule which would deny exemption to a subsidiary in reorganization whose securities were guaranteed by a registered holding company. The effect of such a rule would be to remove Pittsburgh Railways' exempt status.

The agency advised interested parties that the proposed rule would be primarily applicable to Pittsburgh Railways. That Commission invited comments, views, written data and oral argument on the proposed rule, but denied Philadelphia's request for a hearing. The District of Columbia Court of Appeals held that the S.E.C. had improperly denied a trial type of hearing, holding that the agency action was adjudicatory because it was particular and immediate.

In our opinion the *Philadelphia* case is distinguishable from the one now before us. The regulations here in question were promulgated for general and prospective application. They were not, as in *Philadelphia*, directed primarily to a particular company with respect to a matter then pending. The circumstances which led the District of Columbia Circuit to hold that the proceeding was adjudicatory in nature are not present here.[35]

We conclude that the summary rejection, without hearing, of Superior's rate and certificate filings here in issue, did not deprive the company of procedural due process of law.

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[35] Since *Philadelphia* is distinguishable, we need not decide whether we would reach the same result under the facts of that case. But see 1 Davis, Administrative Law Treatise, § 7.01, pages 409-410, commenting upon that decision.

This brings us to a consideration of Superior's arguments directed to whether the Commission had substantive authority to proscribe the price-changing clauses in question and, if so, whether the exercise of that authority by the promulgation of the challenged rules, or in the application of those rules in this case, was in violation of the Act, unreasonable, arbitrary, capricious and discriminatory. Most of the arguments advanced under this branch of the case would have equal relevance if the Commission action had resulted from an *ad hoc* decision instead of from the application of general Commission rules.

Under the statutory scheme of the Natural Gas Act, Superior contends, independent producers have the right to enter into contracts to sell casinghead gas and, in connection therewith, to fix the initial rates for such gas and the conditions under which those rates may be changed in the future. The statute does not, Superior urges, require that future rate changes receive advance approval, or even the filing of rate proposals, but only notice to the Commission before rate changes may be put into effect. These statutory principles, Superior argues, are violated by a proscription upon price-changing clauses of the kind here in question, whether such proscription is the result of an *ad hoc* decision, or of general rule-making.

The Act permits the relations between the parties to be established initially by contract. Among the terms of such contracts are those governing the initial price to be charged. Unless there is provision in such a contract for price changes in the future, both seller and buyer are contractually bound by the initial price, and may not unilaterally obtain a price change even with the consent of the Commission. *United Gas Pipe Line Co.* v. *Mobile Gas Serv. Corp.*, 350 U.S. 332.

It is therefore usual for such contracts to contain price changing clauses. In the case of a producer, such clauses manifest the buyer's consent to a filing under section 4(d) of the Act for the purpose of effectuating a rate change in keeping with the price-changing clause. If the increase is challenged, the producer must still establish its lawfulness wholly apart from the terms of the price-changing clause. *Wisconsin* v. *Federal Power Comm'n*, 273 U.S. 294.

When a producer, as in this case, applies to the Commission, under section 7 of the Act, for a certificate of convenience and necessity authorizing it to sell natural gas in interstate commerce, the Commission must give consideration to the initial price provided for in the contract, and other contract terms relating to initial or future prices. *Atlantic Ref. Co.* v. *Public Service Comm'n* (Catco) 360 U.S. 378, 391; *United Gas Improvement Co.* v. *Federal Power Comm'n*, 9 Cir., 283 F. 2d 817, 823, *cert. denied*, 365 U.S. 879. In *Catco* the Court stated that while under these circumstances, the Commission is not required to determine that the proposed initial price is just and reasonable, there should at least be "a most careful scrutiny and responsible reaction to initial price proposals of producers under § 7." 360 U.S. at 391. It seems to us that, in such a certificate proceeding, the Commission is likewise empowered to scrutinize and react with respect to price-changing clauses in the contract which may trigger future rate filings.

If the Commission disapproves of the proposed initial price, it may grant the certificate only on condition that the price be changed. As stated earlier in this opinion, Superior obtained its present certificate only by accepting a reduction in its proposed initial rate. See notes 1 and 4. If a natural gas company does not find such a rate condition acceptable, it is not compelled to initiate the proposed service. See *Catco*, at 387-388. We see no reason why these principles

are not as applicable to price-changing clauses in the contract filed in support of the certificate application, as to clauses therein, specifying the initial price.

We reach the same conclusion with regard to the regulation of rates under section 4 (relating to new rate filings) and section 5 (relating to rates already in effect). Section 5(a) specifically authorizes the Commission to determine the just and reasonable "rate, charge, classification, rule, regulation, practice, or *contract* to be thereafter observed and in force, and shall fix the same by order. . . ." (Emphasis supplied.) 15 U.S.C. § 717d(a). Section 4 does not make specific references to "contracts." But section 4(e) provides that the Commission may make such orders with reference thereto "as would be proper in a proceeding initiated after it had become effective," (15 U.S.C. § 717c(e)) thereby giving application to section 5(a) quoted above.[36]

Superior calls attention to the fact that for five years, after the 1956 decision in *United Gas Pipe Line Co.* v. *Mobile Gas Serv. Corp.* (Mobile), 350 U.S. 332, the Commission requested, in its annual reports, legislation which would outlaw favored-nation price escalation clauses.

An unsuccessful attempt by an administrative body to secure an express grant from Congress is significant in determining whether the power so requested was conferred by the statute sought to be amended or supplemented. *Federal Trade Comm'n* v. *Bunte Bros., Inc.*, 312 U.S. 349, 351-352.

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[36] In a practical sense, although perhaps not technically, only section 7 certificate authority is involved here. If the Commission, in the exercise of that authority, grants an application for a certificate only upon condition that proscribed price-changing clauses are deleted, the Commission will not be called upon to consider, under sections 4 or 5, the appropriateness of those clauses.

What was requested of Congress in the Commission's annual reports, however, went far beyond the power which the Commission exercised in promulgating the challenged regulation. The requested legislation would have outlawed price escalation clauses in existing contracts, whereas the Commission regulation has only prospective application.

The Commission may well have had doubts about its power to strike such clauses from existing contracts, either by general rule or *ad hoc* decision, without having a like doubt about its power to promulgate a general rule outlawing such clauses only for the future. The fact that Congress was unwilling to set aside, by statutory fiat, existing price escalation clauses, has no tendency to establish that the Commission did not already have power to deal with the problem prospectively after administrative consideration of the respective merits of the various kinds of price escalation clauses.

We recognize that sections 4, 5 and 7, in addition to providing substantive authority with regard to certificate and rate regulation, also specify procedures to be followed, including the necessity of hearings, in exercising that authority. We have heretofore held, however, that with respect to the particular exercise of substantive authority represented by the Commission regulations here in question, that agency was free to proceed under its general rule-making power rather than case by case.

Superior contends that the proscription of the particular price-changing provisions here in question, however accomplished, is unreasonable, arbitrary, capricious and discriminatory, and that, to accomplish such proscription by general rule-making is, for that reason alone, unreasonable, arbitrary and capricious.

In *Pan American Petroleum Corp. v. Federal Power Comm'n*, 10 Cir., 317 F. 2d 796, the Court stated that the summary rejection, without hearing, of a contract containing price-changing clauses, pursuant to the proscription of Rule 154.93, deprived the Court of any record upon which the rejection may be sustained. Pointing out that, upon motion of the Commission, Order No. 242, promulgating the amended form of rule 154.93, had been held not subject to Court review, the Court expressed the view that the Commission had, in practical effect, circumvented Court review of the basic question — the propriety of indefinite price-changing clauses.

We analyze the problem differently. In determining the propriety of rules of general application, only a legal question is presented — whether on the factual premise upon which the Commission acted, the rule promulgated is unreasonable, arbitrary, capricious or discriminatory. If the factual premise itself were open to review, then it would be necessary for all general rule-making to include a trial-like hearing. As stated earlier in the opinion, this is not required.

If there were facts which entitled Superior to a waiver of the rule, it would have been entitled to an evidentiary hearing on that question, and the factual support for any finding resulting from such a hearing would be subject to Court review. But no such hearing was here requested.

We turn to the specific grounds relied upon as showing that the rule proscribing the price-changing clauses before us, and rejecting in advance any filing containing them, is unreasonable, arbitrary, capricious and discriminatory.

Superior points out that the new filing only has the effect of applying, to the new acreage, price-changing clauses already in effect in the same contract with the same buyer

(El Paso), pertaining to the same field (Aneth Field). The company argues that all facts which justified the original certificate still exist and are of greater weight since no extension of the buyer's facilities will be required to take delivery of the new gas.

Since granting the previous certificates and thereby sanctioning the same price-changing provisions, the Commission has, through its studies, experience, and its findings in the *Pure Oil* case, 25 F.P.C. 333, come to the conclusion that such clauses are, and impliedly always have been, contrary to the public interest. This conclusion is as applicable to clauses now in effect with respect to certificated operations as to clauses proposed to be applied to newly-dedicated areas. While the rule reaches only the latter, this was the result of a procedural choice. It does not represent a determination that, to the extent now effective, such clauses are in keeping with the public interest.

Superior argues that a price-changing provision giving the buyer's consent to the purchaser to seek rate increases is fair, reasonable and lawful. To hold otherwise, the company contends, amounts to a prejudging of unknown future conditions and facts upon unknown evidentiary standards. Superior asserts that the outlawed provisions cannot possibly result in any price which is not just and reasonable and which is not related to the economic needs of the seller, because future rate filings designed to take advantage of such provisions, are subject to section 4 of the Act.

In our opinion the Commission had a reasonable basis for proscribing price-changing provisions of the kind before us, and the determination to do so was not arbitrary and capricious.

In its Order No. 242, 27 F.P.C. 339-341, the Commission stated that it intended the proscription thereby accom-

plished to be "rationally related to a condition which requires correction if regulatory objectives embraced by the statute are to be achieved." (*Id.* at 340). This was a proper objective. See *American Trucking Assn's* v. *United States*, 344 U.S. 298, 310, 314.

As its principal reason for outlawing some kinds of indefinite price escalation clauses the Commission stated in its order:

> ". . . Increases in producer prices, triggered by indefinite escalation clauses, have resulted in a flood of almost simultaneous filings. These filings bear no apparent relationship to the economic requirements of the producers who file them. The Natural Gas Act contemplates that prices, to be just and reasonable, be related to economic needs. . . ."

27 F.P.C. at 340.

As an additional reason the Commission stated that the presence of such clauses in contracts on file with the Commission place such an administrative burden upon the Commission as to interfere with the performance of more important Commission functions. This portion of the Commission order is quoted in note 16 above.

In order No. 242, the Commission also referred to, and adopted, its conclusions stated in the *Pure Oil* case, 25 F.P.C. 383, with regard to the undesirable characteristics of such clauses. In its decision in that case, the Commission stated that such clauses are contrary to the public interest in a number of ways. They are, the Commission said, inherently unreasonable because they may be triggered by circumstances which have nothing to do with revenue needs or the reasonableness of rates.[37] Moreover, the Commission

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[37] As to this, the Commission said, in its *Pure Oil* decision, at page 389:

> ". . . As indicated previously, under Pure's provisions, the company's prices are subject to triggering if El Paso

determined in that case, such clauses have an injurious effect which cannot be fully overcome by resort to the refund provision of the Act.[38]

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pays any other producer within the specified area a higher price. There need be no economic or other substantial justification for the increase; the mere fact that a higher price is paid to some other producer would be sufficient to activate the increase. In our view, such an artificial ground for a proposed increase, operating in such a mechanical and arbitrary manner, and lacking any substantial relationship to the factors which bear on the value of gas or on a determination of a reasonable level of rates for it, does not constitute a proper basis for filing proposed increased rates or a sufficient justification for our giving effect to such a filing, at least if the rate contained therein is in excess of those in our producer price Policy Statement 61-1, as amended. And although other types of indefinite escalation provisions are triggered by other kinds of mechanisms, they are in principle subject to these same objections." (Footnote omitted.)

[38] On this point the Commission said, at pages 389-390:

"The injury resulting from the practical effects of these clauses is exemplified by the evidence in this record. Thus, evidence adduced by El Paso indicates that escalation increases under clauses like those of Pure if activated by West Texas' sales will total some 18 million dollars annually. Furthermore, El Paso states that the filing of such increases for its gas supply will require the company to file for proposed increases in its rates. And it points out that by reason of spiral escalation clauses in its contracts with Phillips Petroleum Company, Phillips is entitled to and probably will file for an increase based upon El Paso's increase to its customers. Since Phillips will be permitted to collect this increase under refund obligation, says El Paso, once again the other producers will be entitled to file for increased rates under their escalation provisions and the cycle will start anew.[7] [[7]Under contractual amendments, the spiral escalation clauses have been eliminated from Phillips' contracts.] According to El Paso, if the Pure rate increases here sought become effective, El Paso's gas purchase costs directly and indirectly will be increased in amounts ranging from $35 million to $51 million annually, in excess of El Paso's rate increases sought in its rate filing in Docket No. G-17929."

In the light of these Commission determinations, and with due regard to the experience, expertise, and neutral position of the Commission as a regulatory agency, we find nothing in Superior's arguments advanced here which would warrant a holding that the Commission acted unreasonably, arbitrarily or capriciously in proscribing the clauses involved in our case. Nor do we find anything in Superior's argument which would justify a conclusion that effectuation of the proscription by rule-making rather than *ad hoc* decisions, itself constitutes unreasonable, arbitrary or capricious action.

Superior contends that the regulations are discriminatory because pipelines are not subjected to the same regulations.

We agree with the Comission that a mere difference in treatment, by rule, of pipelines and producers does not invalidate a regulation. Section 1 of the Act, 15 U.S.C. § 717o, specifically provides that

> ". . . for the purpose of its rules and regulations, the Commission may classify persons and matters within its jurisdiction and prescribe different requirements for different classes of persons or matters."

Although the Natural Gas Act was enacted in 1938, the Commission did not undertake to regulate independent producers until after *Phillips Petroleum Co.* v. *Wisconsin*, 347 U.S. 672, was decided in 1954. Since then the Commission's regulations have, in large measure, accorded different treatment to independent producers than to the long-regulated pipeline companies.[39]

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[39] As the Commission states in its brief:

> ". . . Thus the filing requirements in both certificate and rate proceedings are much less detailed for independent producers than for pipelines. Compare Sections 154.1 through 154.86 of the Commission's Regulations under the Natural Gas Act, 18 C.F.R. 154.1-154.86, with Sections

154.91 through 154.103, 18 C.F.R. 154.91-103 (relating to rates); also compare Sections 157.5 through 157.22, 18 C.F.R. 157-5-157.22, with 157.23 through 157.31, 18 C.F.R. 157.23-157.31 (relating to certificates). Similarly, while a uniform system of accounts has been prescribed for pipeline companies of all sizes, none has been adopted for producers, and there are different requirements with respect to annual reports. . . ."

The Commission could well determine that there are practical differences between the operations of the two kinds of companies, which warrant different treatment with regard to price-changing clauses. Pipelines, unlike producers, do not ordinarily seek rate increases for sales to individual distributing companies, but instead file company-wide increases to reflect over-all increased costs in the operations. Such company-wide increases, moreover, are required by the applicable regulations to be supported at the time of filing by substantial cost data amounting to a full factual justification of the new rate.[40] Producers, by contrast, as the Commission points out, not only have continued to establish rates by individual contract but, in addition, their increased rate filings normally relate to such contracts or at most, to only a small portion of their total operation.

In holding that the proscription of price-changing clauses here in question is not unreasonable, arbitrary, capricious or discriminatory, we wish to once again emphasize that we so hold only with regard to the kind of clauses incorporated in the contract here at issue, and in the absence of any showing by Superior that special circumstances exist entitling it to a waiver of the rule.

Other contentions advanced by Superior, not discussed above, have been considered and determined by us to be without merit.

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[40] 18 C.F.R. (1963 Cum. Supp.) § 154.63.

The Letter-Order of June 25, 1962, summarily rejecting the filings referred to therein, thereby giving effect to section 154.93 of the regulations, as amended by Order No. 242. is affirmed.

It is further ORDERED that the petition for rehearing en banc, filed herein on September 19, 1963, be and the same is hereby denied.

(Endorsed) Opinion Filed Aug. 26, 1963, as amended by order of Sept. 25, 1963.

UNITED STATES COURT OF APPEALS
FOR THE NINTH CIRCUIT

THE SUPERIOR OIL COMPANY,
Petitioner,
v.
FEDERAL POWER COMMISSION,
Respondent.

(Endorsed)
Filed
OCT 15 1963
Frank H. Schmid, Clerk
No. 18252

DECREE

Before: POPE, HAMLEY and BROWNING, Circuit Judges.

THIS CAUSE came on for hearing on petition of the Superior Oil Company filed October 5, 1962 to review an order dated June 15, 1962 of the Federal Power Commission, and on the transcript of record, briefs of respective parties, and oral argument had thereon on May 6, 1963.

On August 26, 1963, the Court being fully advised in the premises, handed down its decision affirming the order of the Federal Power Commission. In conformity therewith, it is hereby

ORDERED, ADJUDGED AND DECREED by the United States Court of Appeals for the Ninth Circuit that the said order of the Federal Power Commission in this cause be, and hereby is affirmed.

APPENDIX B

ORDER REJECTING FILINGS

FEDERAL POWER COMMISSION
Washington 25, D.C.

Docket No. G-15431
The Superior Oil Company

JUN 15 1962

The Superior Oil Company
909 R.C.A. Building
1725 K Street, N.W.
Washington 6, D.C.

Attention: Mr. H. J. Penn

Gentlemen:

This is with reference to your letter of May 25, 1962, submitting (1) a supplemental agreement dated April 9, 1962, dedicating additional acreage, for filing as a proposed supplement to your FPC Gas Rate Schedule No. 77 and (2) a related petition to amend the order granting certificate in Docket No. G-15431 to include thereunder the additional acreage.

The additional sale is proposed to be made pursuant to a supplemental agreement dated April 9, 1962, which, in effect, incorporates by reference the terms of a contract dated June 11, 1958. The supplemental agreement appears, therefore, to incorporate by reference pricing provisions other than those permitted by Section 154.93 of the Commission's Regulations. Therefore, in accordance with Commission Order No. 242 (copy enclosed), and Section 154.100 of the Commission's Regulations, the proposed rate sched-

ule supplement and related petition to amend are hereby rejected. All available copies are returned herewith.

This rejection is without prejudice to the resubmittal of the subject filings upon deletion of the unacceptable provisions.

Very truly yours,

J. H. GUTRIDE
Secretary

Enclosure No. 84993

cc: H. W. Varner, Attorney
The Superior Oil Company
P. O. Box 1521
Houston 1, Texas

El Paso Natural Gas Company
P. O. Box 1492
El Paso, Texas

APPENDIX C

The pertinent provisions of the Natural Gas Act of June 21, 1938, c. 556, 52 Stat. 821; as amended by Act of February 7, 1942, c. 49, 56 Stat. 83; June 25, 1948, c. 646, 62 Stat. 991; May 24, 1949, c. 139, 63 Stat. 107; August 28, 1958, Pub. L., 85-791, 72 Stat. 947; 15 U.S.C. 717-717w, are as follows:

1. Section 4:

Rates and Charges; Schedules; Suspension of New Rates

Sec. 4 (a) All rates and charges made, demanded, or received by any natural-gas company for or in connection with the transportation or sale of natural gas subject to the jurisdiction of the Commission, and all rules and regulations affecting or pertaining to such rates or charges, shall be just and reasonable, and any such rate or charge that is not just and reasonable is hereby declared to be unlawful.

(b) No natural-gas company shall, with respect to any transportation or sale of natural gas subject to the jurisdiction of the Commission, (1) make or grant any undue preference or advantage to any person or subject any person to any undue prejudice or disadvantage, or (2) maintain any unreasonable difference in rates, charges, service, facilities, or in any other respect, either as between localities or as between classes of service.

(c) Under such rules and regulations as the Commission may prescribe, every natural-gas company shall file with the Commission, within such time (not less than sixty days from the date this act takes effect) and in such form as the Commission may designate, and shall keep open in convenient form and place for public inspection, schedules showing all rates and charges for any transportation or sale subject to the jurisdiction of the Commission, and the classifications, practices, and regulations affecting such

rates and charges, together with all contracts which in any manner affect or relate to such rates, charges, classifications, and services.

(d) Unless the Commission otherwise orders, no change shall be made by any natural-gas company in any such rate, charge, classification, or service, or in any rule, regulations, or contract relating thereto, except after thirty days' notice to the Commission and to the public. Such notice shall be given by filing with the Commission and keeping open for public inspection new schedules stating plainly the change or changes to be made in the schedule or schedules then in force and the time when the change or changes will go into effect. The Commission, for good cause shown, may allow changes to take effect without requiring the thirty days' notice herein provided for by an order specifying the changes so to be made and the time when they shall take effect and the manner in which they shall be filed and published.

(e) Whenever any such new schedule is filed the Commission shall have authority, either upon complaint of any State, municipality, or State commission, or upon its own initiative without complaint, at once, and if it so orders, without answer or formal pleading by the natural-gas company, but upon reasonable notice, to enter upon a hearing concerning the lawfulness of such rate, charge, classification, or service; and, pending such hearing and the decision thereon, the Commission, upon filing with such schedules and delivering to the natural-gas company affected thereby a statement in writing of its reasons for such suspension, may suspend the operation of such schedule and defer the use of such rate, charge, classification, or service, but not for a longer period than five months beyond the time when it would otherwise go into effect: *Provided*, That the Commission shall not have authority

to suspend the rate, charge, classification, or service for the sale of natural gas for resale for industrial use only; and after full hearings, either completed before or after the rate, charge, classification, or service goes into effect, the Commission may make such orders with reference thereto as would be proper in a proceeding initiated after it had become effective. If the proceeding has not been concluded and an order made at the expiration of the suspension period, on motion of the natural-gas company making the filing, the proposed change of rate, charge, classification, or service shall go into effect. Where increased rates or charges are thus made effective, the Commission may, by order, require the natural-gas company to furnish a bond, to be approved by the Commission, to refund any amounts ordered by the Commission, to keep accurate accounts in detail of all amounts received by reason of such increase, specifying by whom and in whose behalf such amounts were paid, and, upon completion of the hearing and decision, to order such natural-gas company to refund, with interest, the portion of such increased rates or charges by its decision found not justified. At any hearing involving a rate or charge sought to be increased, the burden of proof to show that the increased rate or charge is just and reasonable shall be upon the natural-gas company, and the Commission shall give to the hearing and decision of such questions preference over other questions pending before it and decide the same as speedily as possible. [52 Stat. 822 (1938); 15 U.S.C. §717c]

2. Section 5:

Fixing Rate and Charges; Determination of Cost of Production or Transportation

Sec. 5. (a) Whenever the Commission, after a hearing had upon its own motion or upon complaint of any State,

municipality, State commission or gas distributing company, shall find that any rate, charge, or classification demanded, observed, charged, or collected by any natural-gas company in connection with any transportation or sale of natural gas, subject to the jurisdiction of the Commission, or that any rule, regulation, practice, or contract affecting such rate, charge, or classification is unjust, unreasonable, unduly discriminatory, or preferential, the Commission shall determine the just and reasonable rate, charge, classification, rule, regulation, practice, or contract to be thereafter observed and in force, and shall fix the same by order: *Provided, however,* That the Commission shall have no power to order any increase in any rate contained in the currently effective schedule of such natural-gas company on file with the Commission, unless such increase is in accordance with a new schedule filed by such natural-gas company; but the Commission may order a decrease where existing rates are unjust, unduly discriminatory, preferential, otherwise unlawful, or are not the lowest reasonable rates.

3. Section 7:

Extension of Facilities; Abandonment of Service

Sec. 7 (c) No natural gas company or person which will be a natural-gas company upon completion of any proposed construction or extension shall engage in the transportation or sale of natural gas, subject to the jurisdiction of the Commission, or undertake the construction or extension of any facilities therefor, or acquire or operate any such facilities or extensions thereof, unless there is in force with respect to such natural-gas company a certificate of public convenience and necessity issued by the Commission authorizing such acts or operations: *Provided, however,* That if any such natural-gas company or prede-

cessor in interest was bona fide engaged in transportation or sale of natural gas, subject to the jurisdiction of the Commission, on the effective date of this amendatory Act, over the route or routes or within the area for which application is made and has so operated since that time, the Commission shall issue such certificate without requiring further proof that public convenience and necessity will be served by such operation, and without further proceedings, if application for such certificate is made to the Commission within ninety days after the effective date of this amendatory Act. Pending the determination of any such application, the continuance of such operation shall be lawful.

In all other cases the Commission shall set the matter for hearing and shall give such reasonable notice of the hearing thereon to all interested persons as in its judgment may be necessary under rules and regulations to be prescribed by the Commission; and the application shall be decided in accordance with the procedure provided in subsection (e) of this section and such certificate shall be issued or denied accordingly: *Provided, however*, That the Commission may issue a temporary certificate in cases of emergency, to assure maintenance of adequate service or to serve particular customers, without notice or hearing, pending the determination of an application for a certificate, and may by regulation exempt from the requirements of this section temporary acts or operations for which the issuance of a certificate will not be required in the public interest. [52 Stat. 825 (1938), as amended, 56 Stat. 83 (1942); 15 U.S.C. § 717f (c)]

(d) Application for certificates shall be made in writing to the Commission, be verified under oath, and shall be in such form, contain such information, and notice thereof shall be served upon such interested parties and

in such manner as the Commission shall, by regulation, require. [56 Stat. 84 (1942); 15 U.S.C. § 717f (d)]

(e) Except in the cases governed by the provisos contained in subsection (c) of this section, a certificate shall be issued to any qualified applicant therefor, authorizing the whole or any part of the operation, sale, service, construction, extension, or acquisition covered by the application, if it is found that applicant is able and willing properly to do the acts and to perform the service proposed and to conform to the provisions of the Act and the requirements, rules, and regulations of the Commission thereunder, and that the proposed service, sale, operation, construction, extension, or acquisition, to the extent authorized by the certificate, is or will be required by the present or future public convenience and necessity; otherwise such application shall be denied. The Commission shall have the power to attach to the issuance of the certificate and to the exercise of the rights granted thereunder such reasonable terms and conditions as the public convenience and necessity may require. [56 Stat. 84 (1942); 15 U.S.C. § 717f (e)]

4. Section 16:

Administration Powers of Commission; Rules, Regulations, and Orders

Sec. 16. The Commission shall have power to perform any and all acts, and to prescribe, issue, make, amend, and rescind such orders, rules, and regulations as it may find necessary or appropriate to carry out the provisions of this act. Among other things, such rules and regulations may define accounting, technical, and trade terms used in this act; and may prescribe the form or forms of all statements, declarations, applications, and reports to be filed with the Commission, the information which

they shall contain, and the time within which they shall be filed. Unless a different date is specified therein, rules and regulations of the Commission shall be effective thirty days after publication in the manner which the Commission shall prescribe. Orders of the Commission shall be effective on the date and in the manner which the Commission shall prescribe. For the purposes of its rules and regulations, the Commission may classify persons and matters within its jurisdiction and prescribe different requirements for different classes of persons or matters. All rules and regulations of the Commission shall be filed with its secretary and shall be kept open in convenient form for public inspection and examination during reasonable business hours. [52 Stat. 830 (1938); 15 U.S.C. § 717o]

5. Section 19:

Rehearing; Court Review of Orders

Sec. 19 (b) Any party to a proceeding under this act aggrieved by an order issued by the Commission in such proceeding may obtain a review of such order in the circuit court of appeals of the United States for any ciruit wherein the natural-gas company to which the order relates is located or has its principal place of business, or in the United States Court of Appeals for the District of Columbia, by filing in such court, within sixty days after the order of the Commission upon the application for rehearing, a written petition praying that the order of the Commission be modified or set aside in whole or in part. A copy of such petition shall forthwith be transmitted by the clerk of the court to any member of the Commission and thereupon the Commission shall file with the court the record upon which the order complained of was entered, as provided in section 2112 of Title 28. Upon the filing of such petition such court shall have jurisdiction, which upon the filing of

the record with it shall be exclusive, to affirm modify, or set aside such order in whole or in part. No objection to the order of the Commission shall be considered by the court unless such objection shall have been urged before the Commission in the application for rehearing unless there is reasonable ground for failure so to do. The finding of the Commission as to the facts, if supported by substantial evidence, shall be conclusive. If any party shall apply to the court for leave to adduce additional evidence, and shall show to the satisfaction of the court that such additional evidence is material and that there were reasonable grounds for failure to adduce such evidence in the proceedings before the Commission, the court may order such additional evidence to be taken before the Commission and to be adduced upon the hearing in such manner and upon such terms and conditions as to the court may seem proper. The Commission may modify its findings as to the facts by reason of the additional evidence so taken, and it shall file with the court such modified or new findings, which if supported by substantial evidence, shall be conclusive, and its recommendation, if any, for the modification or setting aside of the original order. The judgment and decree of the court, affirming, modifying, or setting aside, in whole or in part, any such order of the Commission, shall be final, subject to review by the Supreme Court of the United States upon certiorari or certification as provided in sections 239 and 240 of the Judicial Code, as amended (U.S.C., title 28, secs. 346 and 347). (52 stat. 831 (1938); 62 Stat. 991; 63 Stat. 107; 72 Stat. 947; 15 U.S.C. § 717r).

* * *

APPENDIX D

ORDER NO. 232

AMENDING THE COMMISSION'S GENERAL RULES AND REGULATIONS

(18 CFR 154.91(a) and 154.93)

(Issued March 3, 1961)

In this proceeding, the Commission has under consideration a proposed amendment of § 154.93 of its General Rules and Regulations (18 CFR 154.93) respecting the filing of rate schedules containing certain provisions for adjustments in the price of the seller, e.g., "favored nation", "redetermination", and "spiral escalation" clauses.

General public notice of this proposed rule-making was given by publication in the Federal Register on April 12, 1956 (21 FR 2388) and mailing notices to interested parties, including State and Federal regulatory agencies.[1]

In response to such notice, numerous suggestions and comments were submitted by interested parties respecting the changes in the Commission's rules therein proposed. All such suggestions and comments have been carefully considered, but, for reasons set forth in our findings, we adhere to the rule as originally proposed with certain changes made thereto.

The Commission finds:

(1) The natural gas industry and natural gas service are aided and developed by the use of long-term contracts

[1] This issue was also fully tried, briefed, and argued before the Commission in *The Pure Oil Company*, Docket No. G-17930, in which decision is being issued this day.

for the sale of natural gas by producers to pipeline companies or to others, and it is desirable and appropriate in the public interest that long-term contracts be utilized as a basis for considerations of supply and service expansions by natural gas companies.

(2). Long-term gas supply contracts containing provisions for rate changes dependent or based in part on "indefinite escalation clauses", as herein defined, have contributed to instability and uncertainty concerning prices of gas and service expansion by natural gas companies. As found by us in the proceeding of *The Pure Oil Company*, Docket No. G-17930, Opinion No. 341 issued concurrently herewith, these indefinite escalation provisions are contrary to the public interest. Such escalation provisions, therefore, are undesirable, unnecessary, and incompatible with the public interest for the due and proper development of natural gas service by natural gas companies.

(3) It is necessary and appropiate in the public interest and in the proper administration of the Natural Gas Act that § 154.91 (a) of our General Rules and Regulations (18 CFR 154.91(a)) be amended to include definitions of "definite escalation clause" and "indefinite escalation clause" to define clearly the amendment necessitated by our findings in subparagaph (2) hereof.

The Commission, acting pursuant to authority granted by the Natural Gas Act, particularly Sections 4, 7, and 16 thereof (15 U.S.C. 717c, 717f, and 717o); *orders*:

(A) Part 154, entitled Rate Schedules and Tariffs and Subchapter E — Regulations Under Natural Gas Act, Chapter I of Title 18, Code of Federal Regulations, is amended as follows:

(1) In § 154.91(a), change the caption "Definition" to read *"Definitions (1)"* and adding subparagraphs (2) and (3) to read:

"(2) 'Definite escalation clause' means any provision in an independent producer's contract for the sale of natural gas in interstate commerce for resale or the transportation of natural gas in interstate commerce which sets forth the price to be paid for natural gas delivered thereunder in terms of a specific price per unit, including, in addition to the initial price, any increases therein by specific amounts at definite future dates, or any provision which changes the specific price in order to reimburse the seller for all or any part of the changes in production, severance, or gathering taxes levied upon the seller.

"(3) 'Indefinite escalation clause' means any provision, other than a definite escalation clause as defined in subparagraph (2) hereof, under which the price in a contract for the sale or transportation of natural gas by an independent producer subject to the jurisdiction of the Commission may be determined or changed."

(2) Adding a proviso at the end of § 154.93, *Rate schedule defined*, to read as follows:

"*Provided*, That any provision for a change of price of the seller by reason of indefinite escalation clauses, as defined in § 154.91 (a)(3), contained in a contract for the sale or transportation of natural gas subject to the jurisdiction of the Commission tendered for filing on and after April 1, 1961, shall be inoperative and of no effect at law."

(B) These amendments shall become effective April 3, 1961. Any interested person may submit to the Commission on or before March 20, 1961, views or comments in writing concerning these amendments.

(C) The Secretary of the Commission shall cause publication of this order to be made in the Federal Register.

By the Commission. Commissioner Kline, concurring in part and dissenting in part, filed a separate statement.

(Seal)

J. H. Gutride
JOSEPH H. GUTRIDE,
Secretary.

KLINE, Commissioner, *concurring* in part and *dissenting* in part.

I concur completely in the rule insofar as it renders void and inoperative favored nation, spiral escalation and price redetermination clauses in future contracts. I feel such clauses are definitely contrary to the public interest when appearing in gas contracts subject to our regulation.

I am opposed to the rule insofar as it renders void and inoperative provisions in producer contracts permitting price changes arrived at through negotiation or arbitration after a period of five years from the date of the contract. The broad definition of the term "indefinite escalation clause" contained in the rule would eliminate these as well as other unspecified contractual provisions.

It is the practice in the industry for producers to enter into long term contracts for the sale of gas. Such contracts usually run for twenty years or the life of the field which may be fifty or more years. The Commission encourages such long term contracts and this order itself contains a finding that they are in the public interest. It is impossible for anyone to predict the accuracy the economic conditions so far in the future, what the costs of a producer will be at that time, or what will constitute a just and reasonable price for gas. Yet under the law a natural gas company is

bound by its contract and may not unilaterally file for increased rates. *United Gas Pipe Line Co.* v. *Memphis*, 358 U.S. 103, *United Gas Pipe Line Co.* v. *Mobile*, 350 U.S. 322. Under such circumstances a producer should have a contractual right to renegotiate his contract price at some time in the future in order to project himself against inflation or other unforeseen contingencies. He should not be compelled to agree at the beginning of his contract to a fixed price for the gas twenty or fifty years in the future, when conditions may be wholly different.

Many producers have already substituted such negotiation and arbitration clauses in their contracts in lieu of the favored nation and spiral escalation clauses. We have never had a hearing on the issue of whether such provisions are contrary to the public interest, the majority has failed to give any reason for outlawing them, and I can see no reason why we should not permit them.

A contract providing for re-negotiation of the price at some future date, and for arbitration in event the parties fail to agree, merely gives the producer the right to file for such price. The Commission will, of course, disallow it in event it is not a just and reasonable price. Since the gas is already committed to the pipeline, the producer will not have any distinct bargaining advantage. If anything, he will be at a disadvantage, and I see no reason to fear that excessive prices will result, even during the temporary suspension period, as a result of a negotiation and arbitration clause.

I appreciate the difficulty we have in stabilizing gas prices and I would have no objection to a rule finding that it is in the public interest to eliminate even the right to negotiate for a period during which we can reasonably expect economic conditions not to undergo too radical a change, such as a five year period.

In the Memphis case, *supra*, the Supreme Court sustained the contention of this Commission that a natural gas company should have the contractual right to file for an increase even though the amount of the increase is not specifically stated in the contract. We cannot arbitrarily abolish that right but can do so only if the contractual provision supplying the right is against the public interest.

Finally, the adoption of such a broad rule seems to me to be extremely short sighted. Once a rule such as this is adopted, the average business man, as a matter of self-preservation, will seek to avoid its effects. Here the producer will undoubtedly seek to protect himself by increasing the initial price or providing for steeper escalations or through some other means. We impliedly put our blessing on definite escalation clauses regardless of the amount. I consider a contract provision calling for a five cent escalation every five years far worse than a contract provision calling for a one cent escalation with the additional provision for negotiations. Yet the adoption of such a rule as this cannot help but lead to some such results.

In summary, I am opposed to the rule as written because we have never published notice of any intention to adopt such a rule, no showing has been made that all outlawed clauses are against the public interest, and I believe a producer should not be required as his peril to attempt to set prices twenty years in the future, but should be afforded some reasonable means of negotiating a price at a time when he knows the conditions with which he will be faced.

ARTHUR KLINE
Arthur Kline, Commissioner

APPENDIX E

(18 CFR 154.93)

ORDER NO. 232A

ORDER MODIFYING ORDER AMENDING THE COMMISSION'S GENERAL RULES AND REGULATIONS

(Issued March 31, 1961)

On March 3, 1961, the Commission issued its Order No. 232 in this proceeding amending Sections 154.91 (a) and 154.93 of the Regulations under the Natural Gas Act (18 CFR 154.91 (a) and 154.93). The order provided that indefinite escalation clauses, contained in producer contracts filed on and after April 3, 1961, for the jurisdictional sale or transportation of gas, shall be inoperative and of no effect at law. Since March 3, interested persons have submitted views and comments concerning the amendments to our regulations. Upon consideration of such comments and upon our own further consideration, we find it necessary and appropriate to modify the amendments promulgated by Order No. 232.

We reaffirm our earlier findings that the use of long-term contracts for the sale of natural gas by producers to pipelines or to others is desirable and appropriate in the public interest but that indefinite escalation provisions are, in general, contrary to the public interest. However, it also appears that elimination of all indefinite escalation provisions would be too restrictive to enable the industry adequately to cope with possible changing economic conditions over the span of long-term contracts. Therefore, to permit pricing flexibility and to provide an incentive for long-term contracts, we should permit future contracts to contain limited price-redetermination provisions, invocable not

more than once in every five-year contract period and based upon rates subject to this Commission's jurisdiction (and therefore, controlled).

Also upon reconsideration, it appears that the amendments by their terms apply to any contract filed with the Commission on or after April 3, 1961, even if the contract was executed prior to April 3. The amendments should be changed to apply only to contracts executed on or after April 3, 1961.

We hereby *modify* our Order No. 232, issued March 3, 1961, in this proceeding, in the following manner *and order*:

(A) Paragraphs (2) and (3) of the Commission's findings are changed to read as follows:

(2) Gas supply contracts containing provisions for rate changes dependent or based in whole or part on indefinite escalation clauses such as favored-nation, unlimited redetermination or renegotiation, spiral escalation, inflationary adjustment, price indices and revenue-sharing clauses have contributed to instability and uncertainty concerning prices of gas and service expansion by natural gas companies. As found by us in the proceeding of *The Pure Oil Company*, Docket No. G-17930, Opinion No. 341, these indefinite escalation provisions are in general contrary to the public interest. Such escalation provisions, therefore, are generally undesirable, unnecessary and incompatible with the public interest for the due and proper development of natural gas service by natural gas companies. However, limited price-redetermination provisions appear appropriate to meet the difficulty of pricing for long and unpredictable periods and to encourage the negotiation of long term contracts. Limited price-redetermination provi-

sions, as hereinafter ordered, appear to be in the public interest and should be permitted in producer contracts for the sale or transportation of natural gas subject to our jurisdiction.

(3) It is necessary and appropriate in the public interest and in the proper administration of the Natural Gas Act that § 154.93 of the Regulations under the Natural Gas Act (18 CFR 154.93) be amended to specify the change of price provisions that may be contained in future producer rate schedules submitted for filing with this Commission.

(B) Paragraph (A) of the Commission's Order No. 232 is changed to read as follows:

(A) Part 154, entitled Rate Schedules and Tariffs, Subchapter E — Regulations under the Natural Gas Act, Chapter I of title 18, Code of Federal Regulations, is amended by adding a proviso at the end of § 154.93, *Rate schedule defined*, to read as follows:

"*Provided*, That in contracts executed on or after April 3, 1961, for the sale or transportation of natural gas subject to the jurisdiction of the Commission, any provision for a change of price other than the following provision shall be inoperative and of no effect at law; the permissible provisions for a change in price are:

(1) provisions that change a price in order to reimburse the seller for all or any part of the changes in production, severance, or gathering taxes levied upon the seller;

(2) provisions that change a price to a specific amount at a definite date; and

(3) provisions that, once in five-year contract periods during which there is no provision for a change in price to a specific amount [paragraph (2)], change a price at a definite date by a price-redetermination based upon and not higher than a producer rate or producer rates which are subject to the jurisdiction of the Commission, are not in issue in suspension or certificate proceedings, and are in the area of the price in question.

(C) This amendment shall become effective April 3, 1961.

(D) The Secretary of the Commission shall cause publication of this order to be made in the Federal Register. By the Commission. Commissioner Kline would further modify the order to permit renegotiation clauses in conformity with the views expressed in his statement accompanying Order No. 232 issued March 3, 1961.

JOSEPH H. GUTRIDE,
Secretary.

APPENDIX F

ORDER NO. 242

AMENDING REGULATIONS UNDER THE NATURAL GAS ACT

(18 CFR 154.93, 157.14, 157.25)

(Issued February 8, 1962)

In this proceeding the Commission has under consideration the amendment of §§ 154.93, 157.14(a)(10) Exhibit H (v), and 157.25, Subchapter E, Regulations Under the Natural Gas Act, Chapter I of Title 18, Code of Federal Regulations.

By Order No. 232A, issued March 31, 1961 (26 F.R. 2850, 25 FPC 609), the Commission amended section 154.93 of its Regulations so as to provide that indefinite price escalation clauses in sales contracts executed on or after April 3, 1961, for the sale or transportation of natural gas subject to the jurisdiction of the Commission, would be inoperative and of no effect at law. The amendments herein adopted provide for (1) the rejection of contracts containing such indefinite escalation clauses, (2) the rejection of applications by producers for certificates of public convenience and necessity relying for a gas supply upon contracts containing such indefinite escalation provisions, and (3) the Commission's refusal to consider such contracts submitted in support of certificate applications by pipeline companies.

Public notice of proposed rulemaking was given by publication in the Federal Register on October 10, 1961 (26 F.R. 9732), and by mailing copies thereof to interested persons, including natural gas companies, and to State and Federal agencies. In response to such notice, numerous comments were submitted. These comments have been care-

fully considered but, for the reasons set forth below, we adhere to the substance of the amendments as originally proposed.

A number of parties contend that the promulgation of these regulations would be unlawful and beyond the powers granted to the Commission by the Natural Gas Act. We conclude, however, that sections 4, 5, and 7 of the Natural Gas Act contemplate that the Commission will refuse to approve contractual provisions found adverse to the public interest. Section 16 of the Act, of course, authorizes the Commission to issue rules and regulations of general applicability found necessary or appropriate to carry out the provisions of the Act.

Protection of the public interest is the touchstone of our regulatory powers under the Natural Gas Act. The Commission's obligation under the Act to the natural gas companies, as one segment of the public whose interest is to be protected, does not compel it to acquiesce in the use of contracts which carry provisions incompatible with a scheme of effective rate regulation. To be sure, the proposed rule will have impact upon contractual practices which have been fairly widespread. But the real issue is not one of "freedom of contract"; the question is whether the rule is rationally related to a condition which requires correction if regulatory objectives embraced by the statute are to be achieved. See *American Trucking Associations* v. *United States*, 344 U.S. 298. In our view, the rule we adopt fully meets this test.

We held in the *Pure Oil* case[1] that indefinite escalation clauses are contrary to the public interest and restated this conclusion in Order No. 232A. Increases in producer prices, triggered by indefinite escalation clauses, have resulted in a flood of almost simultaneous filings. These filings bear

[1] *The Pure Oil Company*, 25 FPC 383.

no apparent relationship to the economic requirements of the producers who file them. The Natural Gas Act contemplates that prices, to be just and reasonable, be related to economic needs. The elimination of indefinite escalation provisions does not, of course, cut off other avenues by which a producer may make provision for filing for increased rates.

Filings under indefinite escalation clauses have created a significant portion of the administrative burdens under which this Commission is laboring today. The Natural Gas Act contemplates that rate increases shall be sought when there is economic justification, but not that there shall be a chain reaction in a wide area whenever one producer in the area negotiates a contract at a new price level. The Act requires the Commission to give precedence to the hearing and decision of rate increases, but the complexity of indefinite price clauses requires it to spend an undue amount of time in their interpretation and application at the expense of making a prompt determination of the rate issues involved. Accordingly, in protecting the public against waves of increases which have no defensible basis, we also serve the need — which we believe we should take into account — of making the tasks of regulation more manageable.

It has been brought to our attention that section 154.93 of the Regulations, as amended by Order No. 232A, refers to the date of execution of a contract, rather than the filing date (to which we referred in the notice of this proceeding). It is suggested that this point should be clarified. The Commission agrees and has made appropriate changes. In order to conform the language of the amendments to our existing regulations, we have also changed the phrase "price-escalation provisions" to "price-changing provisions".

The Commission, acting pursuant to authority granted by the Natural Gas Act, particularly sections 4, 5, 7, and 16

thereof (15 U.S.C. 717c, 717d, 717f, and 717o), *orders* that Parts 154 and 157, Subchapter E, Chapter I, of Title 18 of the Code of Federal Regulations be amended as follows:

(A) § 154.93 *Rate Schedule Defined,* is amended by adding a provision at the end thereof to read:

> *Provided further,* That any contract executed on or after April 2, 1962, containing price-changing provisions other than the permissible provisions set forth in the proviso next above shall be rejected.

(B) § 157.14(a)(10) *Exhibit H — Total Gas Supply Data* (v), is amended by adding a proviso at the end thereof to read:

> *Provided, further, however,* That any contract executed on and after April 2, 1962, and filed in support of an applicant's gas supply showing will be given no consideration in determining adequacy of gas supply if it contains any price-changing provisions other than those defined as permissible in § 154.93 hereof.

(C) § 157.25 *Necessary exhibits, Exhibit B, Contracts,* is amended by deleting all the language after the first sentence thereof, ending with the words "Natural Gas Act", and inserting in lieu thereof the following:

> On or after April 2, 1962, the application shall be rejected if any contract submitted in support thereof contains any price-changing provisions other than those defined as permissible in § 154.93 hereof.

(D) These amendments shall become effective on April 2, 1962.

(E) The Secretary of the Commission shall cause prompt publication of this order to be made in the Federal Register.

By the Commission. Commissioner O'Connor not participating.

JOSEPH H. GUTRIDE,
Secretary.

APPENDIX G

FEDERAL POWER COMMISSION RULES OF PRACTICE AND PROCEDURE

1.7 PETITIONS

(b) *For issuance, amendment or repeal of rules.* A petition for the issuance, amendment, or repeal of a rule by the Commission shall set forth clearly and concisely petitioner's interest in the subject matter, the specific rule, amendment, or repeal requested, and cite by appropriate reference the statutory provision or other authority therefor. Such petition shall set forth the purpose of, and the facts claimed to constitute the grounds requiring, such rule, amendment, or repeal, and shall conform to the requirements of §§ 1.15 and 1.16. Petitions for the issuance or amendment of a rule shall incorporate the proposed rule or amendment.

In the Supreme Court of the United States

OCTOBER TERM, 1963

No. 684

THE SUPERIOR OIL COMPANY, PETITIONER

v.

FEDERAL POWER COMMISSION

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE NINTH CIRCUIT

MEMORANDUM FOR THE FEDERAL POWER COMMISSION

OPINION BELOW

The opinion of the Court of Appeals (Pet. App. 1a–40a) is reported at 322 F. 2d 601.

JURISDICTION

The judgment of the Court of Appeals was entered on August 26, 1963 (Pet. App. 41a). A timely petition for rehearing was denied on September 25, 1963 (Pet. App. 40a) and the petition for a writ of certiorari was filed on December 18, 1963. The jurisdiction of this Court is invoked under 28 U.S.C. 1254(1) and Section 19(b) of the Natural Gas Act, 15 U.S.C. 717r(b).

716-843—63

QUESTIONS PRESENTED

The Federal Power Commission summarily rejected an application for a certificate of public convenience and necessity filed by petitioner, a gas producer, because it was based upon a contract containing price-changing provisions of a kind which the Commission had proscribed by regulation as contrary to the public interest. The questions presented are:

1. Whether the Commission may, as held by the court below, exercise its rulemaking power in order to prohibit contractual arrangements (including spiral escalation clauses, favored-nation provisions and other types of indefinite pricing) which it finds incompatible with the public interest.

2. Whether the Commission's regulations, which limit the types of price-changing provisions that may be included in producer contracts, are reasonable insofar as they proscribe favored-nations and unlimited-price-redetermination clauses of the kind included in petitioner's rejected filings.

STATUTE INVOLVED

Pertinent provisions of the Natural Gas Act and of the Commission's regulations are set forth in the petition at pages 45a–69a.

STATEMENT

The decision below affirmed the Commission's order rejecting, without hearing, an application for a certificate of public convenience and necessity filed by petitioner, an independent producer of natural gas, and the related proposed rate schedule, which were

based on an April 9, 1962, contract containing price-changing provisions other than those allowed by the Commission's regulations (Pet. App. 1a–5a, 40a).

The Commission's Regulations under the Natural Gas Act, Section 154.91 *et seq.*, as amended (18 C.F.R. (Cum. Supp. 1963) 154.91 *et seq.*), provide that independent producers subject to the agency's jurisdiction shall file their contracts as rate schedules. Section 154.93 provides in part:

> * * * That in contracts executed on or after April 3, 1961, for the sale or transportation of natural gas subject to the jurisdiction of the Commission, any provision for a change of price other than the following provisions shall be inoperative and of no effect at law; the permissible provisions for a change in price are:
>
> (a) Provisions that change a price in order to reimbuse the seller for all or any part of the changes in production, severance, or gathering taxes levied upon the seller;
>
> (b) Provisions that change a price to a specific amount at a definite date; and
>
> (c) Provisions that, once in five-year contract periods during which there is no provision for a change in price to a specific amount (paragraph (b) of this section), change a price at a definite date by a price-redetermination based upon and not higher than a producer rate or producer rates which are subject to the jurisdiction of the Commission, are not in issue in suspension or certificate proceedings, and, are in the area of the price in question * * *.

This language was added by Order No. 232, issued March 3, 1961 (Pet. App. D, pp. 53a–58a; 25 FPC 379; 26 Fed. Reg. 1983), as amended by Order No. 232A, issued March 31, 1961 (Pet. App. E., pp. 59a–62a; 25 FPC 609; 26 Fed. Reg. 2850).

Section 154.93 of the regulations further provides that "any contract executed on or after April 2, 1962, containing price-changing provisions other than the permissible provisions" described above "shall be rejected." Similarly, Section 157.25 provides that an independent producer's application for a certificate of public convenience and necessity "shall be rejected" if any contract submitted in support of it contains the forbidden provisions. These provisions were added to the regulations by Order No. 242, issued February 8, 1962 (Pet. App. F, pp. 63a–67a; 27 FPC 339; 27 Fed. Reg. 1356).[1]

The April 9, 1962, agreement incorporated by reference the provisions of a 20-year contract entered into by Superior and El Paso in 1958. The pricing terms adopted by the 1962 agreement called for an initial price of 20 cents per Mcf for the first five years commencing with the date of initial delivery under the original contract, 21 cents per Mcf for the second five-year period, 22 cents per Mcf for the third five-year period, 23 cents for the fourth five-year period, and

[1] The procedural background of these regulations is described at pp. 2–8 of the Commission's petition in *Federal Power Commission* v. *Texaco Inc., et al.*, No. 386, this Term, certiorari granted on November 12, 1963, 375 U.S. 902, to which we respectfully refer the Court.

24 cents per Mcf thereafter if the contract is still in effect. The initial price was reduced to 17.7 cents per Mcf, in accordance with a condition attached to the certificate issued by the Commission for sale under the 1958 contract. In addition to these permissible fixed-price escalation provisions, the agreement also provided for a price redetermination for each five-year period after the first, and included a so-called favored-nation clause providing that El Paso would never pay petitioner less than the price it was paying "others for comparable gas delivered under comparable conditions" within a specified area. (Pet. App. 3a–4a.)

After the Commission's rejection based on the regulations, petitioner sought rehearing, urging that the summary rejection of its applications was invalid because (1) the regulations upon which the Commission relied were invalid, (2) the regulations and the rejection order were improperly issued without opportunity for hearing, and (3) in any event, the Commission cannot, even in a rate or certificate proceeding, modify provisions of contracts which "do not affect the initial 'rate charge or classification'" (R. 126). Petitioner recognized that its contract contained proscribed price-changing provisions and it made no request for a waiver of the regulations.

The Court below affirmed, holding that the Commission had properly exercised its substantive powers by rule-making and that it had a reasonable basis for proscribing price-changing provisions of the kind involved here.

DISCUSSION

This case deals with the same regulations involved in *Federal Power Commission* v. *Texaco, Inc.*, No. 386, in which certiorari was granted on November 12, 1963, 375 U.S. 902. As we pointed out in the supplemental memorandum to our petition in No. 386, there is a direct and express conflict between the *Texaco* decision and the decision in the instant case as to the Commission's power to proceed by rule or regulation (Question 1, *supra*). As to this issue, therefore, there is no question as to the propriety of granting the writ.

Nor do we oppose consideration of the further question decided below, but not reached in Texaco, *i.e.*, whether the rules, as applied, were a reasonable exercise of the Commission's authority. To be sure, as to this issue there is no conflict at the present time. But the reasonableness of the rules presents a question related to the scope of the Commission's rule-making power. Moreover, as noted in our petition in No. 386, the regulations in question are nationwide in their application and constitute an important element in the Commission's effort to achieve effective regulation of producers. Finally, we point out that the same issue is involved in litigation in the Fifth and Tenth Circuits, and that a definitive resolution by this Court would relieve uncertainty and contribute to the sound administration of the Natural Gas Act.

CONCLUSION

For the foregoing reasons, we do not oppose certiorari. We also suggest that, if the writ is granted, it would be appropriate to set the case for argument with No. 386.

Respectfully submitted.

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1963

No. 684

THE SUPERIOR OIL COMPANY, *Petitioner*

v.

FEDERAL POWER COMMISSION, *Respondent*

PETITION FOR REHEARING OF ORDER DENYING PETITION FOR WRIT OF CERTIORARI

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IN THE

Supreme Court of the United States

OCTOBER TERM, 1963

No. 684

THE SUPERIOR OIL COMPANY, *Petitioner*

v.

FEDERAL POWER COMMISSION, *Respondent*

PETITION FOR REHEARING OF ORDER DENYING PETITION FOR WRIT OF CERTIORARI

Now comes THE SUPERIOR OIL COMPANY (Petitioner), and petitions for rehearing of Order of this Court entered May 4, 1964, dismissing its Petition For Writ of Certiorari to review judgment of the United States Court of Appeals For The Ninth Circuit reported in 322 F.2d 601. In support hereof Petitioner shows as follows:

I.

This Court's Order of May 4, 1964, undoubtedly results from the Court's view that its decision and judgment rendered April 20, 1964, in Cause No. 386 of the current term, *Federal Power Commission v. Texaco, Inc., et al.*,

as related to Pan American was dispositive of the instant Petition For Writ of Certiorari. Such is not the case. The instant Petition raised two fundamental questions, i.e.:

(1) The inherent rule-making authority of the Commission.[1]

(2) Whether Order No. 242, if within the general rule-making power of the Commission, is a reasonable, and therefore valid, exercise of such rule-making power.[2]

The Court's decision in No. 386 dealt only with the first point and that based on amendment of the Commission's Rules of Practice and Procedure adopted subsequent to Commission action herein. No. 386 in no wise dealt with the second issue above and this is apparent from the Petition For Writ therein, the Briefs in support thereof, the oral argument presented to the Court, and the decision.[3]

---

[1] Questions Presented I-IV, and see Part II hereof.

[2] Questions Presented V(b) and (c):
"May the Federal Power Commission under the Natural Gas Act and its authority to make rules necessary or appropriate to carry out the provisions of that Act validily promulgate a general rule which *** (b) does not reasonably accomplish the stated purpose of the rule and (c) is unreasonable, arbitrary, capricious and discriminatory in application." (Petition for Writ Pg. 4.)

[3] **Petition** (The Questions Presented)—"Whether the Commission may proceed by way of the rule making power to prohibit contractual arrangements *** which it finds incompatible with the public interest ***." (Petition No. 386, Pg. 2.)

Brief—"Without reaching the question of the reasonableness of the Commission's indefinite-pricing regulations the decision below, held them invalid on the ground that the subject is one the Commission cannot deal with by general rule but must decide case by case. While we shall, therefore, not discuss their

Only the inherent rule-making power of the Commission was involved. That the nature of the second issue raised by this Petition is separate and distinct from that of inherent rule-making power of the Commission is fully recognized in "Memorandum For The Federal Power Commission" filed by the Solicitor General herein. Rephrasing Petitioner's above statement of said second issue, said "Memorandum" posed the same issue under "Questions Presented" as follows:

> "2. Whether the Commission's regulations, which limit the types of price changing provisions that may be included in producer contracts, are reasonable insofar as they proscribe favored nation and unlimited-price-redetermination clauses of the kind included in Petitioner's rejected filings." (Memorandum Pg. 2.)

The potential unreasonableness of Order No. 242 in its application was directly pointed to in the Petition For Writ:

> "The Commission action was arbitrary and unreasonable. The Commission requires long term (20 years plus) contracts to assure the gas supply to the purchaser

---

reasonableness, we think it will be helpful to set the regulations against the background of the problems which led to their promulgation." (Solicitor General's Brief, No. 386, Pg. 15.)

Oral Argument—"The Court below set aside the Commission's regulations on the ground the regulations were invalid. Not because they were unreasonable. The Court didn't reach that question." Solicitor Wahrenbrock, Ward & Paul Tr. Pg. 4, Oral Argument: "I refer to it (Pure Oil opinion) not to argue the reasonableness of the regulations because that question was not passed on by the Court below and we have not attempted to argue it in our briefs here ***." (ID. Pg. 6.)

Decision—"We think *** that the statutory requirement for a hearing under Section 7 does not preclude the Commission from particularizing statutory standards through the rule making process ***." (Slip Opn. Pg. 6.)

> pipelines. * * * and now predict, at the producers' (not the Commission's) risk, what such conditions and the needs of the producers will be for 20 years. It is said that favored nation filings bear no apparent relationship to the economic requirements of the producers who file them. This ignores the internal competitive nature of the oil industry." (Petition Pg. 17.)

The importance of this issue to the Commission, to the companies regulated, and to the public was recognized in the Solicitor's said "Memorandum", i.e.:

> "Nor do we oppose consideration of the further question decided below, *but not reached in Texaco*, i.e. whether the rules, as applied, were a reasonable exercise of the Commission's authority. To be sure, as to this issue there is no conflict at the present time. *But the reasonableness of the rules presents a question related to the scope of the Commission's rule-making power* * * *. The regulations in question are nationwide in their application and constitute an important element in the Commission's effort to achieve effective regulation of the producers. Finally, we point out that the same issue is involved in litigation in the Fifth and Tenth Circuits. and that a definitive ruling by this Court would relieve uncertainty and contribute to the sound administration of the Natural Gas Act." (Memorandum Pg. 6. Emphasis added.)

Highlighting this point and bringing into sharp focus the reasonableness of Order No. 242, in its present application, is a decision by the Fifth Circuit Court rendered March 26, 1964, not yet officially reported, No. 20642, *Zara Foster, et al. v. The Atlantic Refining Company*,[4]

[4] Printed in full insofar as said decision relates to this point. Appendix Pages i to ix post.

which holds that a gas producer who fails to include flexible pricing clauses of the type proscribed by Order No. 242 does so at his peril. This was a suit by royalty owners for an accounting for royalty due from the sale of gas. The oil and gas lease, held by Atlantic, provided that royalties payable on gas were:

> "1/8 of that produced and saved from said land, * * * to be sold at the market price therefor prevailing for the field where produced when run * * *."

Atlantic, in 1950, entered into a 20-year contract for the sale of gas to be produced from the lease. The gas price provided was 7.018¢ per MCF for the first five-year period, increasing to 8.5¢ and then to 9.4¢ per MCF during successive five-year periods. At the time of contracting, the initial price provided was *higher* than the market price; however, by 1957 the prevailing market price established by other sales had increased to 13¢ per MCF, and for the period 1958 to 1962 the prevailing market price was 14¢ per MCF. Atlantic paid gas royalties on the contract prices. The royalty owners sued and recovered the difference of $75,000 between the contract prices and the higher market prices. Atlantic contended it should not be held responsible for the higher market price because it was impossible for it to provide in its long term contract for day-to-day or even year-to-year market price changes, and its initial contract price exceeded market price at the time of contracting. To this the Court replied:

> "The practicalities of the gas industry require that gas be sold under long-term contracts because the

[1] An interstate gas sale subject to Commission jurisdiction.

pipelines must have a committed source of supply sufficient to justify financing, construction, and operation. The impact of this economic fact on the royalty clause of the Foster-Atlantic lease produces the problem presented here." (App. Pg. III and IV)

* * *

"The impossibility argument is reduced to the question of the possibility of the inclusion in the 1950 contract of escalation provisions which would have assured the lessees the prevailing prices during the periods in question in this suit. * * *" (App. Pg. V)

"* * * The obligation of Atlantic to pay royalties is fixed and unambiguous. It made the gas sales contract with full knowledge of this obligation and did nothing to protect itself against increase in price. The fact that its purchaser would not agree to pay the market price prevailing at the time of delivery does not destroy the lease obligation." (App. Pg. V)

* * *

"Stripped of all the trimmings Atlantic's position is simply: We cannot comply. This is no answer. The lease calls for royalty based on the market price prevailing for the field where produced when run. The fact that the ascertainment of future market price may be troublesome or that the royalty provisions are improvident and result in a financial loss to Atlantic 'is not a web of the Court's weaving.' Atlantic cannot expect the court to re-write the lease to Atlantic's satisfaction." (App. Pg. VII)

The *Foster* case involves a commonplace provision for royalty on gas in oil and gas leases.[6] The *only* method by

[6] Petitioner's lease here involved covers Navajo Indian Lands subject to supervision by the Secretary of Interior. The royalty obligation is based on "value" of the gas. Value is fixed in the

which Atlantic could have protected itself would have been the inclusion in said 20-year contract of the *very type* of flexible pricing provisions proscribed by Commission Order No. 242. *Foster* judicially recognizes that such flexible pricing clauses are absolutely necessary for producer protection in long term gas sales. Such clauses bear both apparent and real relationship to the economic requirements of the producers. Without same a producer's contract is deemed "improvident" and a "web" resulting in financial loss from which a court will grant no relief. Yet these clauses are proscribed by Order No. 242 here under consideration, based on administrative determination, without an evidentiary hearing, that they bear no apparent relation to the economic requirements of producers. This determination is unfounded and is judicially repudiated in the *Foster* case.

II.

In addition to the above, to the extent that the decision in No. 386 relied on the "waiver" provision in the Commissions' Rules of Practice and procedure, Section 1.7(b), to satisfy the statutory requirement for hearing under Section 7 of the Act (No. 386, Slip Opn. Pgs. 6 and 7, FN 11), such decision is not controlling of the instant Petition. The Commission rule quoted in Footnote 11 is an amendment of said regulations which was not in

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Secretary's discretion "*** calculated on the basis of, the highest price paid or offered *** at the time of production for the major portion of *** gas *** sold from the field." The actual amount received by the lessee may be deemed "mere evidence of or conclusive evidence of such value".

Substantially similar royalty provisions are included in all leases from the United States. 43 CFR 192.82 (5)(d). 43 CFR 200.81. 43 CFR 201.41.

effect at the time of the Commission's rejection of the Petitioner's instant application nor when rehearing on said rejection was sought. The Court below so recognized (App. Pg. 6a, instant Petition For Writ). The Commission Regulation, in effect at times relevant to the instant matter, provided only for petition for *issuance, amendment or repeal* of Commission orders or rules, not *waiver*.[7]

The Court below held that "amendment or repeal" permitted by the old rule implicitly included "waiver" and equated Section 1.7(a) of the Commission's Rules to Rules 1.361(c) and 1.702 of the Rules of the Federal Communications Commission which *explicitly* provided for petitions for waiver, and otherwise read much as the Federal Power Commission's now, but not then, *amended* Rule 1.7(b) quoted in No. 386. Clearly 1.7(a) provides only a general right of petition to the Commission, and prescribes formal requirements therefor. The "implicit" meaning of the old rules *after* the amendment was obviously

[7] "1.7 PETITIONS

(a) **General.** Petitions for relief under any statute or other authority delegated to the Commission shall be in writing and under oath, shall state clearly and concisely the petitioner's grounds of interest in the subject matter, the facts relied upon, and the relief sought, and shall cite by appropriate reference the statutory provision or other authority relied upon for relief and shall conform to the requirements of Secs. 1.15 and 1.16.

(b) **For issuance, amendment or repeal of rules.** A petition for the issuance, amendment, or repeal of a rule by the Commission shall set forth clearly and concisely Petitioner's interest in the subject matter, the specific rule, amendment, or repeal requested, and cite by appropriate reference the statutory provision or other authority therefor. Such petition shall set forth the purpose of, and the facts claimed to constitute the grounds requiring, such rule, amendment or repeal, and shall conform to the requirements of Secs. 1.15 and 1.16. Petitions for the issuance or amendment of a rule shall incorporate the proposed rule or amendment."

not implicit before; otherwise the need, which the Commission recognized, for amendment to explicitly permit petitions for *waiver* would not have existed. If any prior *implicit* right to seek waiver may be found, it is submitted that such tenuous and uncertain right to a hearing is no substitute for the clear and express hearing right, and due process of law, unqualifiedly granted by Section 7 of the Natural Gas Act.

PRAYER

WHEREFORE, PETITIONER PRAYS for rehearing of its Petition For Writ of Certiorari, and that upon such rehearing said writ be granted.

Respectfully submitted.

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Attorneys For
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May 14, 1964.

This is to certify that this Petition For Rehearing is presented in good faith and not for delay, and is restricted to intervening circumstances and other substantial grounds not previously presented.

H. W. VARNER
Attorney for Petitioner

May 14, 1964.

APPENDIX

IN THE

United States Court of Appeals

FOR THE FIFTH CIRCUIT

No. 20642

ZARA FOSTER, ET AL.,
Appellants-Appellees,

versus

THE ATLANTIC REFINING COMPANY,
Appellee-Appellant.

(AND REVERSE TITLE)

Appeals from the United States District Court for the Southern District of Texas

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(March 26, 1964.)

Before HUTCHESON, BREITENSTEIN,* and BELL, Circuit Judges.

BREITENSTEIN, Circuit Judge: We have here a complex controversy between lessors and lessee over their respective rights under a Texas oil and gas lease. The issues concern the failure to account for royalties due, to pay com-

*Of the Tenth Circuit, sitting by designation.

pensatory royalties, to produce and market, and to develop. The factual issues were presented to a jury which answered numerous special interrogatories. The trial court gave judgment in favor of the lessors and against the lessee in the sum of $154,931.29. Both sides have appealed.

In 1944 the Fosters, appellees and cross-appellants herein referred to as lessors or as Fosters, gave an oil and gas lease to The Atlantic Refining Company, appellant and cross-appellee herein referred to as lessee or as Atlantic. The lease covered 1,500 acres located in the Hagist Ranch Field, Duval County, Texas. The Hagist Ranch Field is a multi-reservoir field which produces both oil and gas. We shall discuss each appeal and issue separately.

I.

ATLANTIC APPEAL

(a) Failure to account for royalties.

The lessors contend that the lessee has not paid gas royalties to which they are entitled. The royalty clause reads in pertinent part:

> "The conventional royalties to be paid by Lessee are: (a) On oil and gas, including all hydro-carbons, one-eighth (1/8th) of that produced and saved from said land, the same to be delivered to the credit of the Lessor into the pipe line and to be sold at the market price therefor prevailing for the field where produced when run; * * *."

In 1950, lessee made a 20-year gas sales contract with Texas Illinois Natural Gas Pipeline Company covering the

Foster and other leases owned by Atlantic in the Hagist Ranch Field. The prices to be paid by the pipeline company per mcf were:

> "7.0180 cents during the first five year period; 8.5531 cents during the next five year period; and 9.4304 cents during the third five year period.
>
> "For the fourth five year period the price shall be the fair and reasonable value thereof as of the commencement of said period, taking into consideration the price then being paid for gas of similar quantity and quality sold for similar purposes in the general area of the Hagist Ranch Area, provided, however, that in no event shall such price be less than 10.0883 cents for each 1,000 cubic feet of gas."

The uncontroverted evidence is that the price prevailing for the field was 13 cents in 1957 and 14 cents for the period 1958-1962.[1] The Fosters claim that they are entitled to royalties based on these prices rather than on the prices fixed by the 1950 gas sales contract. The trial court agreed with the Fosters and, on this issue, gave them judgment for $75,012.51, the difference between what they were paid and what the court held they should have been paid.

The practicalities of the gas industry require that gas be sold under long-term contracts because the pipelines must have a committed source of supply sufficient to justify

[1] Lessors concede that the 4-year statute of limitations applies, Vernon's Ann. Civ. St. art. 5527, and that they cannot go back beyond four years from the filing of the original complaint in 1961.

financing, construction, and operation.[2] The impact of this economic fact on the royalty clause of the Foster-Atlantic lease produces the problem presented here.

Undisputed testimony for Atlantic is that at the time it made the 1950 contract with Texas Illinois it received a higher initial price and an agreement for a substantially higher daily take of gas than could have been negotiated with the other two pipelines operating in the area.[3] The 13-cent and 14-cent prices on which the Fosters rely were established by the testimony of an expert who directed particular attention to four long-term contracts made in 1949, 1952, and 1956, and are not controverted by Atlantic.

Atlantic says that compliance with the royalty provision of the lease as interpreted by the Fosters and the trial court is impossible. It argues that no pipeline or other purchaser will buy large quantities of gas on a day to day or other short-term basis. In this the jury agreed as it answered in favor of Atlantic interrogatories presenting the questions of the salability of the gas on a day to day, month to month, or year to year basis. As we see the case these factors are immaterial. The Fosters make no claims based on short-term fluctuations in price. Instead they say that the market price of gas in 1957 was 13 cents and in the period 1958-1962 was 14 cents. Atlantic offered no evidence of day to day, month to month, or year to year fluctuations in price. This court said in *Phillips Petroleum Co. v. Bynum*, 5 Cir., 155 F.2d 196, 198, that: "* * * [W]hen seeking market value gas at the well we cannot require the application of rules of daily sales and

---

[2] See Gex v. Texas Company, Tex. Civ. App., 337 S.W.2d 820, 828.

[3] Texas Illinois had not then entered into the area.

daily quotations when there is no showing that such sales and quotations occur." The record conclusively establishes that the market price of the gas prevailing in the field when the gas was delivered to the pipeline was 13 cents in 1957 and 14 cents in the 1958-1962 period.

The impossibility argument is reduced to the question of the possibility of the inclusion in the 1950 contract of escalation provisions which would have assured the lessees the prevailing prices during the periods in question in this suit. Atlantic says, and the jury found, that such provisions could not have been incorporated in a contract having the initial price and delivery quantity agreements contained in the 1950 contract. The Fosters do not dispute this but say that such impossibility is no excuse.

The inability of Atlantic to make a gas sales contract with escalation provisions is beside the point. The obligation of Atlantic to pay royalties is fixed and unambiguous. It made the gas sales contract with full knowledge of this obligation and did nothing to protect itself against increases in price. The fact that its purchaser would not agree to pay the market price prevailing at the time of delivery does not destroy the lease obligation. The case falls within the rule thus stated in *Ellwood v. Nutex Oil Co.*, Tex. Civ. App., 148 S.W.2d 862, 864:

> "* * * [O]ne who unconditionally obligates himself to do a thing possible of performance, must be held to perform it (citing cases); and though performance, subsequent to the contract, may become difficult or even impossible, [this] does not relieve the promisor, and particularly where he might have foreseen the difficulty and impossibility (citing cases)."

When it made the gas sales contract, Atlantic took the calculated risk of that contract producing royalties satisfactory to the lease terms. The fact that increases in market prices have made the lease obligations financially burdensome is no defense.

Atlantic urges that the market price is the price at which the gas was sold in 1950. Developing this point it first says that the phrase "when run" applies to oil but not to gas on the theory that a "run" is a transfer of crude oil from stock tanks to a pipeline.[4] We see no reason why the phrase may not apply to gas and mean the time of delivery of gas from the well to the pipeline. Indeed, a witness for Atlantic so testified.[5]

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[4] See Long v. Magnolia Petroleum Company, 166 Neb. 410, 89 N.W.2d 245, 257.

[5] Atlantic witness Echols testified in part thus:

"Q. But what does the contract say?

A. This contract says to be sold at the market price therefor.

Q. Prevailing in the field?

A. Yes, sir.

Q. When run?

A. That's correct.

Q. When the gas is run, is that right?

A. That's right.

Q. All right. Now that gas is run every day that those wells produce, isn't it?

A. Yes, sir, but that gas is not sold every day when the leases are producing.

* * * * * * *

"Q. All right. Now then, when it says 'gas (sic) run,' let's get to that point next.

A. Well, of course, the terminology 'run' does not actually apply to gas, but I would twist and say it probably refers to it at the time it is delivered to the pipeline.

Q. Now it actually refers to it there, doesn't it?

A. I presume it does."

Atlantic also says that the gas was sold in 1950 for future delivery. The difficulty is that under a Texas decision, *Martin v. Amis*, Tex. Com. App., 288 S.W. 431, 433, the 1950 contract was an executory contract for the sale of gas with an executed sale of gas being effected when the gas came into possession of the pipeline.

Atlantic argues that it is only required to use reasonable diligence in selling the Foster royalty gas and that the 1950 contract was not improvident. These arguments beg the question. The royalty provision is clear. Granting that the 1950 contract was provident when made, that fact does not change the royalty provisions.

Stripped of all the trimmings Atlantic's position is simply: We cannot comply. This is no answer. The lease calls for royalty based on the market price prevailing for the field where produced when run. The fact that the ascertainment of future market price may be troublesome or that the royalty provisions are improvident and result in a financial loss to Atlantic "is not a web of the Court's weaving."[6] Atlantic cannot expect the court to rewrite the lease to Atlantic's satisfaction.

This brings us to the contention of Atlantic that the lessors ratified the 1950 contract by accepting the royalties payable thereunder and are now estopped to claim royalties based on a higher market price. Atlantic relies on the principle that ratification is established where a principal, though having no prior knowledge of the unauthorized acts of

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[6] Phillips Petroleum Co. v. Bynum, 5 Cir., 155 F.2d 196, 198, certiorari denied 329 U.S. 714.

his agent, retains benefits after acquiring full knowledge of those acts.[7]

The accepted principles of agency and estoppel do not apply in the circumstances of this case. Atlantic had the right to make a sales contract for lessors' gas. This contract was valid and the lessors could do nothing about it. In that contract Atlantic warranted its title and agreed to pay royalties "in accordance with the terms of the respective leases." The facts and laws establish the right of the Fosters to a royalty based on a higher price than that provided in the 1950 contract. This court has held that the acceptance by the lessors of less royalty than that to which they were entitled does not "extinguish the entire debt nor work an estoppel."[8] By keeping less than was due them, and something to which they were entitled in any event, the Fosters have not ratified the act of Atlantic in selling their royalty gas for less than the prevailing market price.

Atlantic says that the 4-year statute of limitations bars recovery as the breach, if there was one, occurred in 1950 when the gas sales contract was executed.[9] As previously stated, the 1950 contract was not a present sale of the gas.[10] The Texas rule is that the statute begins to run on money due as royalty under a written contract when such money

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[7] See Blackburn v. Automobile Finance Co., Tex. Civ. App., 121 S.W.2d 388, 389.

[8] Arkansas Natural Gas Corporation v. Sartor, 5 Cir., 98 F.2d 527, 530, certiorari denied 305 U.S. 649.

[9] See Vernon's Ann. Civ. St., art. 5527.

[10] See Martin v. Amis, Tex. Com. App., 288 S.W. 431, 433.

is due and payable.[11] In the case before us the money did not become due and payable until after an executed sale of the gas was made by the delivery of the gas to the pipeline.

The trial court correctly held that the Fosters were entitled to royalty on the prices prevailing in the period 1957-1962.

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[11] See Hickok Producing & Development Co. v. Texas Co., 5 Cir., 128 F.2d 183, 185; Phillips Petroleum Co. v. Johnson, 5 Cir., 155 F.2d 185, 190 certiorari denied 329 U.S. 730.